UNITED STATES
POSTAL REGULATORY COMMISSION
Washington, D.C. 20268-0001

FORM 10-Q

QUARTERLY REPORT PURSUANT TO 39 U.S.C. § 3654 AND SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the Quarterly Period Ended June 30, 2018

UNITED STATES POSTAL SERVICE

(Exact name of registrant as specified in its charter)

Washington, D.C.	41-0760000
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
475 L'Enfant Plaza, S.W.	
Washington, D.C.	20260
(Address of principal executive offices)	(ZIP Code)

(202) 268-2000
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the *Securities Exchange Act of 1934* during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☐ No ☐ Not Applicable ☑

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☐ No ☐ Not Applicable ☑

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ☐	Accelerated filer ☐	Non-accelerated filer ☐
Smaller reporting company ☐	Emerging growth company ☐	Not Applicable ☑

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☑

The number of shares of common stock outstanding as of August 8, 2018: N/A

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

UNITED STATES POSTAL SERVICE
STATEMENTS OF OPERATIONS
(UNAUDITED)

(in millions)	Three Months Ended June 30, 2018	Three Months Ended June 30, 2017	Nine Months Ended June 30, 2018	Nine Months Ended June 30, 2017
Revenue:				
Operating revenue	$ 17,074	$ 16,665	$ 53,722	$ 53,117
Other revenue	3	10	22	27
Total revenue	**17,077**	**16,675**	**53,744**	**53,144**
Operating expenses:				
Compensation and benefits	12,343	12,012	37,713	37,083
Unfunded retirement benefits amortization	778	1,244	2,335	1,983
Retiree health benefits	900	1,418	3,361	3,191
Workers' compensation	206	(29)	172	(794)
Transportation	1,882	1,740	5,940	5,534
Other operating expenses	2,427	2,391	7,487	7,282
Total operating expenses	**18,536**	**18,776**	**57,008**	**54,279**
Loss from operations	**(1,459)**	**(2,101)**	**(3,264)**	**(1,135)**
Interest and investment income	33	17	82	38
Interest expense	(63)	(56)	(182)	(167)
Net loss	**$ (1,489)**	**$ (2,140)**	**$ (3,364)**	**$ (1,264)**

See accompanying notes to the unaudited financial statements.

UNITED STATES POSTAL SERVICE
BALANCE SHEETS

(in millions)	June 30, 2018 (Unaudited)	September 30, 2017
Current Assets:		
Cash and cash equivalents	$ 11,152	$ 10,513
Restricted cash	341	291
Receivables, net	1,258	1,127
Supplies, advances and prepayments	142	134
Total current assets	**12,893**	**12,065**
Property and equipment, net	14,517	14,891
Other assets	484	438
Total assets	**$ 27,894**	**$ 27,394**
Current Liabilities:		
Compensation and benefits	$ 1,870	$ 2,397
Unfunded retirement benefits	5,488	3,153
Retiree health benefits	41,521	38,160
Workers' compensation costs	1,381	1,513
Payables and accrued expenses	2,086	1,930
Deferred revenue-prepaid postage	2,100	2,168
Customer deposit accounts	1,155	1,196
Other current liabilities	1,255	1,210
Current portion of debt	12,800	10,100
Total current liabilities	**69,656**	**61,827**
Workers' compensation costs, noncurrent	15,195	16,397
Employees' accumulated leave, noncurrent	1,870	1,918
Other noncurrent liabilities	1,061	1,076
Noncurrent portion of debt	2,200	4,900
Total liabilities	**89,982**	**86,118**
Net Deficiency:		
Capital contributions of the U.S. Government	3,132	3,132
Deficit since 1971 reorganization	(65,220)	(61,856)
Total net deficiency	**(62,088)**	**(58,724)**
Total liabilities and net deficiency	**$ 27,894**	**$ 27,394**

See accompanying notes to the unaudited financial statements.

UNITED STATES POSTAL SERVICE
STATEMENTS OF CASH FLOWS
(UNAUDITED)

(in millions)	Nine Months Ended June 30, 2018	2017
Cash flows from operating activities:		
Net loss	$ (3,364)	$ (1,264)
Adjustments to reconcile net loss to cash provided by operations:		
Depreciation and amortization	1,247	1,256
(Gain) loss on disposals of property and equipment, net	(15)	6
(Increase) in other assets	(46)	(22)
(Decrease) in noncurrent workers' compensation	(1,202)	(2,212)
(Decrease) in noncurrent deferred appropriations and other revenue	(1)	(92)
(Decrease) increase in other noncurrent liabilities	(32)	86
Changes in current assets and liabilities:		
Receivables, net	(136)	(14)
Other current assets	(8)	(15)
Unfunded retirement benefits	2,335	1,983
Retiree health benefits	3,361	3,191
Payables, accrued expenses and other	(469)	(316)
Deferred revenue-prepaid postage, prepaid box rents and other	(46)	(56)
Net cash provided by operating activities	**1,624**	**2,531**
Cash flows from investing activities:		
Purchases of property and equipment	(905)	(997)
Proceeds from sales of property and equipment	14	45
Net cash used in investing activities	**(891)**	**(952)**
Cash flows from financing activities:		
Issuance of notes payable	52,500	17,100
Payments on notes payable	(52,500)	(17,100)
Payments on capital lease obligations and other	(44)	(49)
Net cash used in financing activities	**(44)**	**(49)**
Net increase in cash, cash equivalents and restricted cash	689	1,530
Cash, cash equivalents and restricted cash at beginning of period	10,804	8,330
Cash, cash equivalents and restricted cash at end of period	**$ 11,493**	**$ 9,860**
Supplemental cash flow disclosures:		
Cash paid for interest	$ 183	$ 160

See accompanying notes to the unaudited financial statements.

NOTES TO UNAUDITED FINANCIAL STATEMENTS

NOTE 1 - BASIS OF PRESENTATION

Interim Financial Statements

The accompanying unaudited interim financial statements of the United States Postal Service (the "Postal Service") have been prepared in accordance with accounting principles generally accepted in the United States ("GAAP") for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of the U.S. Securities and Exchange Commission ("SEC") Regulation S-X. These financial statements should be read in conjunction with the Postal Service's financial statements for the year ended September 30, 2017, included in its Annual Report on Form 10-K ("Annual Report") filed with the Postal Regulatory Commission ("PRC") on November 14, 2017, and do not include all information and footnotes which are normally included in the Annual Report. Except as otherwise specified, all references to years are to the fiscal year beginning October 1 and ending September 30, and quarters are quarters within fiscal years 2018 and 2017.

In the opinion of management, the accompanying unaudited interim financial statements reflect all material adjustments, including recurring adjustments, necessary to fairly present the financial position as of June 30, 2018, the results of operations for the three and nine months ended June 30, 2018, and 2017, and cash flows for the nine months ended June 30, 2018, and 2017. Operating results for the three and nine months ended June 30, 2018, are not necessarily indicative of the results that may be expected for all of 2018. Mail volume and revenue are historically greatest in the first quarter of the fiscal year, which includes the holiday mailing season.

Reclassifications

Certain reclassifications have been made to the financial statements as of and for the three and nine months ended June 30, 2017, to conform to the current period presentation. Specifically, certain retirement benefit expenses have been reclassified from *Compensation and benefits* and separately identified as *Unfunded retirement benefits amortization* within *Operating expenses* in the accompanying unaudited *Statements of Operations.* In addition, the liabilities associated with these retirement benefits have been reclassified from *Compensation and benefits* and separately identified as *Unfunded retirement benefits* within *Current liabilities* in the accompanying *Balance Sheets*. Corresponding reclassification occurred within *Changes in current assets and liabilities* in the accompanying unaudited *Statements of Cash Flows*. These reclassifications had no effect on previously reported operating expenses, loss from operations or net loss.

Recently Issued Accounting Pronouncements

Accounting Standards Update 2014-09 Revenue from Contracts with Customers

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update 2014-09 *Revenue from Contracts with Customers* ("ASU 2014-09"). The new standard outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. The new standard may be adopted either retrospectively or on a modified retrospective basis whereby the new standard would be applied to new and existing contracts with remaining performance obligations as of the effective date, with a cumulative catch-up adjustment recorded to beginning retained earnings or net deficiency at the effective date for existing contracts with remaining performance obligations.

The new standard becomes effective for the Postal Service's 2019 fiscal year (beginning October 1, 2018) and the quarters therein. The Postal Service is in the process of evaluating the impact of the standard. As of the date of this filing, the Postal Service has completed its identification of revenue streams to determine which streams require further analysis. The Postal Service has completed its contract analysis based on the five-step model as outlined in the authoritative literature.

The Postal Service is utilizing a comprehensive approach to assess the impact of the guidance on its contract portfolio by reviewing its current accounting policies and practices to identify potential differences that would result from applying the new requirements to its revenue contracts, including evaluation of transfer of control, multiple-element arrangements, free goods, breakage and variable consideration. The Postal Service intends to use the modified retrospective approach. The Postal Service is currently quantifying the impact of the standard and does not currently expect the adoption to have a material impact on its financial statements.

Accounting Standards Update 2016-02 Leases

In February 2016, the FASB issued Accounting Standards Update 2016-02 *Leases* ("ASU 2016-02"). The new standard requires an entity to record most leases on its balance sheets but continue to recognize expenses in the statements of operations in a manner similar to current accounting practices. The new standard states that a lessee will recognize a lease liability for the obligation to make lease payments and a right-of-use asset for the right to use the underlying asset for the lease term. Expenses related to leases determined to be operating leases will be recognized on a straight-line basis, while those determined to be finance leases will generally have higher expense in the earlier periods of the lease and both interest and amortization are presented separately in the statements of operations.

ASU 2016-02 will become effective for the Postal Service's 2020 fiscal year (beginning October 1, 2019) and the quarters therein, with early adoption permitted but not elected by the Postal Service. Entities are required to use a modified retrospective approach for leases that exist or are entered into after the beginning of the earliest comparative period in the financial statements. In July 2018, the FASB approved an additional and optional transition method that would allow adoption of the standard as of the effective date without restating prior periods.

The Postal Service has completed its initial scoping exercise and continues to evaluate whether embedded leases exist in its service contracts. In addition, the Postal Service has begun abstracting all of the necessary information to properly account for over 23,000 property leases under the new standard. The Postal Service continues to evaluate the full impact of adopting this standard on its financial statements and disclosures, as well as its impact of adoption on Postal Service policies, practices and systems. As of June 30, 2018, the Postal Service had $7.9 billion of future minimum operating lease commitments that are not currently recognized on its balance sheet. Therefore, the Postal Service expects that the adoption will have a material effect on its balance sheet and disclosures, and limited impact on its statements of operations and statements of cash flows.

Accounting Standards Update 2016-04 Liabilities - Extinguishments of Liabilities

In March 2016, the FASB issued Accounting Standards Update 2016-04 *Liabilities - Extinguishments of Liabilities* ("ASU 2016-04"). The new standard requires entities that sell prepaid stored-value products redeemable for goods, services or cash at third-party merchants to recognize "breakage" (i.e., the value that is ultimately not redeemed by the consumer) as revenue on a pro-rata basis using an estimate based on past redemption patterns, consistent with how gift card breakage will be recognized under ASU 2014-09, discussed earlier.

ASU 2016-04 will become effective for the Postal Service's 2019 fiscal year (beginning October 1, 2018) and the quarters therein, with early adoption permitted. The Postal Service intends to use the modified retrospective approach with a cumulative catch-up adjustment recorded to beginning retained earnings or net deficiency as of the beginning of the fiscal year the standard is effective. The standard is applicable to the Postal Service's determination of outstanding money orders and related escheatment. The Postal Service does not expect the adoption of this standard to have a material impact on its financial statements and disclosures.

NOTE 2 - LIQUIDITY

The Postal Service generates its cash almost entirely through the sale of postal products and services. The Postal Service holds its cash with the Federal Reserve Bank of New York and invests its excess cash, when available, in highly-liquid, short-term investments issued by the U.S. Department of the Treasury. As of June 30, 2018, and September 30, 2017, the Postal Service held unrestricted cash and cash equivalents of $11.2 billion and $10.5 billion, respectively.

Debt

The Federal Financing Bank ("FFB"), a government-owned corporation under the general supervision of the Secretary of the Treasury, holds all of the Postal Service's debt, which consists of fixed-rate notes with various maturities of $11.0 billion and two revolving credit facilities totaling up to $4.0 billion with interest rates determined by the U.S. Department of the Treasury each business day. As of June 30, 2018, and September 30, 2017, these facilities were fully drawn and were included in the current portion of debt. These annually-renewable facilities were renewed on April 20, 2018, and are scheduled to expire and be renewed in April 2019.

As of both June 30, 2018, and September 30, 2017, the aggregate principal balance of all debt outstanding was $15.0 billion, the maximum borrowing amount allowed under the Postal Service's statutory debt ceiling. The Postal Service has reported $15.0 billion in outstanding debt each quarter since September 30, 2012.

Liquidity Concerns

The Postal Service is constrained by laws and regulations, including the *Postal Accountability and Enhancement Act*, Public Law 109-435 ("PAEA"), which restricts revenue sources and mandates certain expenses. Additionally, as noted above, the Postal Service has reached the maximum borrowing capacity under its statutory debt ceiling.

PAEA-mandated expenses include amortization payments to provide full funding of retirement benefits under the Civil Service Retirement System ("CSRS") and the Federal Employee Retirement System ("FERS"), described in greater detail below and in *Note 7 - Retirement Plans*. Additionally, the PAEA established the Postal Service Retiree Health Benefits Fund ("PSRHBF") and mandated certain obligations for paying the normal costs and full prefunding of retiree health benefits. These prefunding obligations are unlike those imposed on most other federal entities or private sector businesses, described in greater detail below and in *Note 8 - Health Benefits Plans*.

The Postal Service reported operating expenses of approximately $72 billion in 2017 and has incurred cumulative net losses of $68.5 billion from 2007 through June 30, 2018. The Postal Service defaulted on $33.9 billion in PSRHBF prefunding payments for the years 2012 through 2016. The Postal Service also did not make $6.9 billion in payments to the Office of Personnel Management ("OPM") by September 30, 2017, for CSRS, FERS and PSRHBF amortization of unfunded liabilities and for the normal cost of retiree health benefits. The Postal Service did not make these payments in order to preserve liquidity and to ensure that its ability to fulfill its primary universal service mission was not placed at undue risk.

As a result of these losses and its liquidity concerns, the Postal Service is unlikely to have sufficient liquidity, absent legislative and regulatory change, to meet all of its existing legal obligations when due, to pay down its debt and to make the critical infrastructure investments that have been deferred in recent years, while fulfilling its statutory universal service obligation. Additionally, the Postal Service believes that continuing productivity improvements and cost reduction measures alone will not be sufficient to address the challenges presented by declining volume and revenue for our Market-Dominant services, and that it is unlikely that revenue growth will keep pace with increased costs driven by network growth, inflationary pressures, contractual agreements and legal mandates.

Business Model Challenges/Constraints

Market-Dominant services, which account for approximately 70% of the Postal Service's annual operating revenues, are currently subject to a price cap as measured by the Consumer Price Index for All Urban Consumers ("CPI-U"). However, the Postal Service's costs are not similarly constrained. A large portion of its cost structure cannot be altered expeditiously due to the Postal Service's universal service obligation, which currently includes a legal requirement to deliver mail six days per week, while the number of delivery points continues to grow by approximately one million per year, further driving up delivery costs. As described above, certain employee and retiree benefit costs are mandated by law and cannot be altered without legislative change. Under current law, the Postal Service is generally unable to increase prices sufficiently to offset increased costs, and is likewise constrained by law from reducing many of its costs or from pursuing many alternate sources of revenue.

Aside from its universal service obligation, a significant factor contributing to Postal Service losses is the ongoing decline in the volume of Market-Dominant services. Specifically, secular declines in *First-Class Mail* are largely the result of changes in consumers' and businesses' use of mail resulting from the continuing migration to electronic communication and transactional alternatives, which has taken place over the last decade and is expected to continue. After experiencing relatively flat volume between 2009 and 2016, beginning in 2017, *Marketing Mail* volume has been challenged by commercial mailers' increasing use of digital advertising. Further exacerbating losses is the increasing number of delivery points, which, when combined with the reduction in mail volume, has resulted in a drop in the average number of pieces delivered per delivery point per day from approximately 5.5 pieces in 2007 to 3.6 pieces in 2017, a decline of approximately 35%.

Because the Postal Service provides its services primarily through its employees, its costs are heavily concentrated in wages and benefits for both current employees and retirees. These costs are significantly impacted by wage inflation, employee health benefit premium increases, and retirement and workers' compensation programs. Some of these costs have historically increased at a higher rate than inflation.

Retirement Benefits and Retiree Health Benefits

Postal Service liquidity may be significantly impacted by its obligations for retirement benefits and retiree health benefits, including obligations for FERS normal costs, RHB normal costs, and unfunded CSRS, FERS and PSRHBF liabilities.

OPM periodically notifies the Postal Service regarding its revaluation of unfunded CSRS and FERS liabilities. OPM calculates these obligations using government-wide economic and demographic data, rather than Postal Service-specific demographics and economic assumptions. In October 2017, OPM issued a new rule announcing its intent to calculate future unfunded CSRS and FERS obligations using Postal Service-specific demographic assumptions. The new rule did not address the use of government-wide versus Postal Service-specific economic assumptions, and therefore did not fully address the Postal Service's concerns.

The Postal Service records CSRS and FERS amortization expenses as *Unfunded retirement benefits amortization* in the accompanying unaudited *Statements of Operations*, and as current liabilities within *Unfunded retirement benefits* in the accompanying *Balance Sheets*. These amounts may be significantly impacted by changes in actuarial assumptions used to revalue the unfunded liabilities. Additionally, the Postal Service is obligated to pay FERS normal costs, representing its employer contributions to the FERS plan for participating employees.

As required by PAEA, OPM annually performs an actuarial valuation for the purpose of developing a payment schedule for the Postal Service to fund the remaining unfunded PSRHBF obligation in annual payments through the year 2056. In addition, the Postal Service is obligated to pay the estimated normal costs of retiree health benefits attributable to the service of its employees during the most recently ended fiscal year.

For additional information regarding retirement benefits and retiree health benefits, see *Note 7 - Retirement Plans* and *Note 8 - Health Benefits Plans*, respectively.

Mitigating Circumstances

The Postal Service continues to pursue strategies within its control to increase operational efficiency and improve liquidity. The Postal Service has conserved capital in recent years by spending only what it believed was essential to maintain its existing facilities and service levels and to increase efficiencies. However, an increase in capital investment is necessary to upgrade its facilities, fleet of vehicles and processing equipment in order to remain operationally viable.

The Postal Service continues to support legislation that will enable it to increase revenue and reduce costs. Specifically, reforms to establish a set of health care plans within the Federal Employees Health Benefits ("FEHB") Program, fully integrated with Medicare, for current and future Postal Service retirees, would eliminate most of the current retiree health benefits unfunded liability and substantially reduce annual amortization and normal cost payment requirements.

The Postal Service's status as an independent establishment of the executive branch that does not receive tax dollars for its operations presents unique requirements and restrictions, but also potentially mitigates some of the financial risk that would otherwise be associated with a cash shortfall. With annual total revenue in 2017 of approximately $70 billion, a financially-sound Postal Service continues to be vital to U.S. commerce.

The U.S. economy benefits greatly from the Postal Service and the many businesses that provide the printing and mailing services that it supports. Disruption of the mail would cause undue hardship to businesses and consumers as it would significantly inhibit the remittance of payments through the mail, and in the event of a cash shortfall, the U.S. government would likely prevent the Postal Service from significantly curtailing or ceasing operations. The Postal Service continues to inform the Administration, Congress, the PRC and other stakeholders of the immediate and long-term financial challenges it faces and the legislative and regulatory changes that are required to restore its financial stability.

NOTE 3 - RELATED PARTIES

As disclosed throughout this report, the Postal Service has significant transactions with other U.S. government entities, which are considered related parties for accounting purposes.

The following table presents related-party assets and liabilities as of June 30, 2018, and September 30, 2017:

(in millions)	June 30, 2018	September 30, 2017
Related-party assets:		
Receivables and advances[1]	$ 72	$ 47
Carrying amount of revenue forgone installment receivable[2]	441	426
Related-party liabilities:		
Current portion of debt	$ 12,800	$ 10,100
Other current liabilities[3]	48,687	43,504
Noncurrent portion of debt	2,200	4,900
Other noncurrent liabilities[4]	15,219	16,420

[1] Current portion within *Receivables, net* and noncurrent portion within *Other assets* in the accompanying *Balance Sheets*.
[2] Included within *Other assets* in the accompanying *Balance Sheets*. See further discussion in *Note 10 - Fair Value Measurement*.
[3] Amounts include CSRS, FERS, PSRHBF and current workers' compensation obligations as well as payables to other agencies.
[4] Amounts include noncurrent workers' compensation obligations.

The following table presents related-party revenue and expenses for the three and nine months ended June 30, 2018, and 2017:

	Three Months Ended June 30,		Nine Months Ended June 30,	
(in millions)	2018	2017	2018	2017
Related-party operating revenue[1]	$ 244	$ 220	$ 744	$ 717
Related-party operating expenses[2]	$ 4,099	$ 5,090	$ 12,852	$ 12,382
Related-party interest income[3]	$ 33	$ 16	$ 82	$ 38
Related-party interest expenses[4]	$ 60	$ 51	$ 170	$ 151

[1] Included within *Operating revenue* in the accompanying unaudited *Statements of Operations*.
[2] Included within *Operating expenses* in the accompanying unaudited *Statements of Operations*.
[3] Imputed on the revenue forgone installment receivable or generated on cash equivalents held with the Federal Reserve Bank of New York or short-term investments in U.S. Treasury instruments. Included within *Interest and investment income* in the accompanying unaudited *Statements of Operations*.
[4] Incurred on debt issued to the FFB, and included within *Interest expense* in the accompanying unaudited *Statements of Operations*.

NOTE 4 - CASH, CASH EQUIVALENTS AND RESTRICTED CASH

The following table provides a reconciliation of cash, cash equivalents and restricted cash reported in the accompanying *Balance Sheets* as of June 30, 2018, and 2017, respectively, and as of September 30, 2017, and 2016, respectively (to disclose the opening balances), that sum to the totals of the same such amounts shown in the accompanying unaudited *Statements of Cash Flows* for the nine months ended June 30, 2018, and 2017:

	June 30,		September 30,	
(in millions)	2018	2017	2017	2016
Cash and cash equivalents	$ 11,152	$ 9,498	$ 10,513	$ 8,077
Restricted cash	341	362	291	253
Total *Cash, cash equivalents and restricted cash* as shown in the accompanying unaudited *Statements of Cash Flows*	**$ 11,493**	**$ 9,860**	**$ 10,804**	**$ 8,330**

Restricted cash represents Postal Service cash that is not available for general use. This includes cash originated from forfeitures or seizures related to consumer fraud or other criminal activity related to the mail and either held for third-party beneficiaries or awaiting disposition. *Restricted cash* also includes funds designated for specific use due to congressional appropriation for Postal Service obligations to the PRC and the United States Postal Service Office of Inspector General, or that is otherwise restricted.

NOTE 5 - PROPERTY AND EQUIPMENT, NET

Assets within *Property and equipment, net* in the accompanying *Balance Sheets* are recorded at cost, which includes the interest on borrowings used to finance construction of major capital additions, less allowances for depreciation and amortization. Interest capitalized during both the three and nine months ended June 30, 2018, and 2017, was not significant. Fixed assets are depreciated over estimated useful lives ranging from 3 to 40 years using the straight-line method.

The net book values of assets classified as held for sale were approximately $10 million and $18 million as of June 30, 2018, and September 30, 2017, respectively, and are included within *Property and equipment, net* in the accompanying *Balance Sheets*.

For the three months ended June 30, 2018, and 2017, depreciation and amortization expense was $421 million and $431 million, respectively, and impairment charges were de minimis. For the nine months ended June 30, 2018, and 2017, depreciation and amortization expense was $1.2 billion and $1.3 billion, respectively, and impairment charges were de minimis. These items are included within *Other operating expenses* in the accompanying unaudited *Statements of Operations*.

NOTE 6 - COMMITMENTS AND CONTINGENCIES

Commitments

In May 2018, the Postal Service agreed to extend contract negotiations on a new collective bargaining agreement with the National Rural Letter Carriers' Association ("NRLCA"). The contract with the NRLCA expired on May 20, 2018, and the respective parties mutually agreed to extend negotiations beyond the deadline.

Contingencies

The Postal Service's contingent liabilities consist primarily of claims resulting from labor, employment, and environmental matters; property damage and injuries on Postal Service properties; and issues arising from Postal Service contracts, personal claims and traffic accidents. Each quarter, the Postal Service evaluates each new claim to determine if it is probable of an unfavorable outcome and if the amount of the potential resolution is reasonably estimable, and if so, a liability for the amount is recorded. Preexisting claims are also reviewed and adjusted quarterly for resolutions or revisions to prior estimates.

The Postal Service has made adequate provision for probable losses arising from all claims. The following table presents contingent liabilities by current and noncurrent portions and by category, as of June 30, 2018, and September 30, 2017:

(in millions)	June 30, 2018	September 30, 2017
Current/noncurrent portions of contingent liabilities:		
Current portion[1]	$ 249	$ 161
Noncurrent portion[2]	516	500
Total contingent liabilities	**$ 765**	**$ 661**
Contingent liabilities by category:		
Labor and employment matters	$ 635	$ 549
Asset retirement obligations	54	54
Tort matters	69	54
Contractual matters	7	4
Total contingent liabilities	**$ 765**	**$ 661**

[1] Included within *Payables and accrued expenses* in the accompanying *Balance Sheets*.
[2] Included within *Other noncurrent liabilities* in the accompanying *Balance Sheets*.

In addition to accruals for probable losses in the financial statements, the Postal Service also has claims which it deems reasonably possible of an unfavorable outcome, which are not accrued for in the financial statements. These ranged in amount from $200 million to $675 million at both June 30, 2018, and September 30, 2017. The Postal Service is from time to time involved in other litigation incidental to the conduct of its business, none of which is expected to be material to its financial condition or operations.

NOTE 7 - RETIREMENT PLANS

The majority of career employees participate in one of two U.S. government defined benefit pension programs, CSRS and FERS, which OPM administers. These plans provide retirement, death and termination benefits for eligible employees based on specific eligibility and participation requirements, vesting periods and benefit formulas. Each employee's participation in either plan is based on the starting date of employment with the Postal Service or another U.S. government entity.

As government-sponsored benefit plans, CSRS and FERS are not subject to the provisions of the *Employee Retirement Income Security Act of 1974*, as amended. Likewise, because the Postal Service cannot direct the costs, benefits or funding requirements of these plans, it accounts for program expenses under multiemployer plan accounting rules. As such, the Postal Service records contributions to the plans as an expense in the period in which each contribution is due.

Career employees may also participate in the Thrift Savings Plan ("TSP"), a defined contribution retirement savings and investment plan administered by the Federal Retirement Thrift Investment Board. The Postal Service's TSP expenses are related only to its contributions for FERS employees who participate in the TSP.

CSRS provides a basic annuity plan benefit to employees hired before January 1, 1984. CSRS Offset provides Social Security benefits in addition to its basic annuity plan for employees hired between January 1, 1984, and January 1, 1987. CSRS and CSRS Offset employees may also participate in the TSP, although the Postal Service does not match contributions for these participants.

From 2007 to 2017, PAEA suspended the Postal Service's employer contributions to CSRS that would otherwise have been required under *Title 5, Section 8334(a)(1)* of the U.S. Code, although CSRS employees continue to contribute to the plan. By law, the Postal Service does not pay normal costs for CSRS retirement benefits; however, in 2017 the Postal Service was required to begin making annual payments to amortize the unfunded CSRS liability.

Effective January 1, 1987, FERS covers employees hired since December 31, 1983, and FERS employees are covered by an annuity, Social Security and TSP benefits. For most FERS employees, OPM has set the Postal Service's normal cost contribution rates at 13.7% of base salary for both 2017 and 2018. For FERS employees who participate in TSP, the Postal Service contributes 1% of basic pay and matches voluntary employee contributions up to an additional 4% of basic pay.

FERS Employees' Current Year Service Expense

The Postal Service records expenses for FERS employees' current year service consisting of FERS normal cost, Social Security and TSP contributions, each of which is included within *Compensation and benefits* in the accompanying unaudited *Statements of Operations*. The following table presents these expenses for the three and nine months ended June 30, 2018, and 2017:

	Three Months Ended June 30,		Nine Months Ended June 30,	
(in millions)	2018	2017	2018	2017
FERS normal costs[1]	$ 871	$ 868	$ 2,609	$ 2,603
Social Security[2]	$ 519	$ 491	$ 1,599	$ 1,536
TSP	$ 276	$ 271	$ 829	$ 812

[1] Represents the Postal Service's employer cash contributions, which excludes employee Social Security contributions and period-end unpaid employer amounts due, for FERS employees.

[2] Represents the Postal Service's Social Security contributions for FERS employees.

CSRS and FERS Unfunded Retirement Benefits Amortization

OPM periodically notifies the Postal Service regarding its revaluation of unfunded CSRS and FERS liabilities. The Postal Service records these expenses as *Unfunded retirement benefits amortization* in the accompanying unaudited *Statements of Operations*. These amounts may be significantly impacted by changes in actuarial assumptions used to revalue the unfunded liabilities.

During the third quarter of 2017, the Postal Service recorded adjustments to its expenses for the amortization of CSRS and FERS unfunded liabilities, due to revised actuarial assumptions. In June 2017, the Postal Service received an invoice from OPM in the amount of $1.7 billion for the first annual CSRS amortization payment due September 30, 2017. The Postal

Service therefore recorded an additional $383 million accrual for the CSRS amortization expense for the three and nine months ended June 30, 2017, to adjust for the increase in the invoiced amount as compared to the previous estimate. Because of OPM's revised actuarial assumptions, the Postal Service updated the estimate of its FERS annual amortization payment due September 30, 2017, to $903 million. This adjustment resulted in an increase in FERS amortization expense of $491 million for both the three and nine months ended June 30, 2017.

OPM calculates these obligations using government-wide economic and demographic data. In October 2017, OPM issued a new rule announcing its intent to calculate future unfunded CSRS and FERS obligations using Postal Service-specific demographic assumptions. The new rule did not address the use of government-wide versus Postal Service-specific economic assumptions, and therefore did not fully address the Postal Service's concerns.

Also in October 2017, OPM provided the Postal Service with an actuarial report indicating the projected amortization payments due September 30, 2018, would be $1.7 billion for the CSRS obligation and $917 million for the FERS obligation. These projected payments did not include the estimated effect of the above-discussed transition to Postal Service-specific demographic assumptions.

In April 2018, the Board of Actuaries of the CSRS, which oversees OPM's calculation of actuarial liabilities for CSRS and FERS, lowered the discount rate used to calculate CSRS and FERS unfunded retirement liabilities from 4.5% to 4.25%. Assuming the use of Postal Service-specific demographic assumptions, the Postal Service has estimated that the impact of this change in discount rate on the annual CSRS and FERS amortization expense will result in revised projected amortization payments due September 30, 2018, of approximately $1.8 billion for the CSRS obligation and approximately $1.3 billion for the FERS obligation, increases of $89 million and $371 million, respectively, from the originally projected amounts.

The Postal Service expects to receive invoices from OPM for the actual amounts due September 30, 2018, during the fourth quarter of 2018, and these may differ from the Postal Service's revised projections due to changes in discount rates, actuarial assumptions and experience as of the calculation date.

The following table presents the expenses recorded for CSRS and FERS unfunded retirement benefits amortization for the three and nine months ended June 30, 2018, and 2017:

	Three Months Ended June 30,		**Nine Months Ended June 30,**	
(in millions)	**2018**	**2017**	**2018**	**2017**
CSRS unfunded liability amortization expense[1]	$ 456	$ 691	$ 1,369	$ 1,306
FERS unfunded liability amortization expense[2]	322	553	966	677
Total CSRS and FERS unfunded retirement benefits amortization	**$ 778**	**$ 1,244**	**$ 2,335**	**$ 1,983**

[1] Expense for the accrual for the annual payment due to OPM by September 30 of the respective fiscal year, to amortize the unfunded CSRS retirement obligation. 2018 amounts are based on updated Postal Service estimates resulting from revised actuarial assumptions. 2017 amounts include an adjustment to reflect an increase in the amount invoiced as compared to OPM's original estimate. Payments are to be made through 2043 based on OPM invoices.

[2] Expense for the accrual for the annual payment due to OPM by September 30 of the respective fiscal year, to amortize the unfunded FERS retirement obligation. 2018 amounts are based on updated Postal Service estimates resulting from revised actuarial assumptions. 2017 amounts include an adjustment to reflect an increase in the amount invoiced as compared to OPM's original estimate. Payments are to be made through 2047 based on OPM invoices.

The amounts the Postal Service has accrued for CSRS and FERS unfunded retirement benefits but has not yet paid are recorded as a current liability within *Unfunded retirement benefits* in the accompanying *Balance Sheets*.

Total expenses related to multiemployer retirement plans include CSRS and FERS unfunded liability amortization, and FERS normal costs. For the three months ended June 30, 2018, and 2017, these expenses totaled $1.6 billion and $2.1 billion, respectively. These amounts show a year-over-year decrease for the quarter due to the prior year expense adjustments discussed above. For the nine months ended June 30, 2018, and 2017, these expenses totaled $4.9 billion and $4.6 billion, respectively.

NOTE 8 - HEALTH BENEFITS PLANS

FEHB covers nearly all career employees and also covers non-career employees and retirees who meet certain eligibility requirements. OPM administers FEHB and allocates the cost of funding the program to participating U.S. government employers. The Postal Service cannot direct the costs, benefits or funding requirements of the plans. Therefore, it accounts for program expenses using multiemployer plan accounting rules by recording contributions to the plans that will be required by OPM as an expense in the period in which the contributions are due. Although OPM determines the actual health benefits premium costs, the allocation of these costs between the Postal Service and most of its employees is determined through agreements with Postal Service labor unions. Separate from FEHB, the Postal Service offers its own healthcare plan to certain non-career employees who are ineligible for FEHB.

Active Employees

The Postal Service paid 72.5% and 73.6% of FEHB premium costs during the three months ended June 30, 2018, and 2017, respectively. The Postal Service paid 72.9% and 73.8% of FEHB premium costs during the nine months ended June 30, 2018, and 2017, respectively. Postal Service employee healthcare expense was approximately $1.3 billion for each of the three months ended June 30, 2018, and 2017. Postal Service employee healthcare expense was approximately $3.9 billion for each of the nine months ended June 30, 2018, and 2017. These expenses are included within *Compensation and benefits* in the accompanying unaudited *Statements of Operations*.

Retirees

Postal Service retirees who participated in FEHB for the five years immediately preceding their retirement may continue to participate in the plan during retirement. Qualifying survivors of retirees are also eligible to receive benefits. The Postal Service is required to contribute to the PSRHBF an amount estimated to be equal to the employer portion of FEHB insurance premiums for participating employees and their qualifying survivors, upon retirement, for each employee's current year of service (normal cost). The Postal Service is also required to contribute an amount sufficient to fully amortize the unfunded liability of the PSRHBF by 2056. These amounts are based, in part, on each current and prospective retiree's length of federal civilian service occurring on or after July 1, 1971. Each participant's share of premium costs is set by law and is not subject to negotiation with Postal Service labor unions. The Postal Service expenses what it is billed by OPM for both normal cost and amortization of the unfunded liability.

The PAEA required the Postal Service to prefund retiree health benefits during years 2007 through 2016 by paying annual amounts ranging from $1.4 billion to $5.8 billion, totaling $54.8 billion, into the PSRHBF, which began paying the Postal Service's share of retiree health benefit premiums in 2017. The Postal Service remains obligated to fund the $33.9 billion in PSRHBF prefunding payments that it defaulted on for the years 2012 through 2016, as well as the amortization and normal cost payments of $955 million and $3.3 billion, respectively, that it did not pay in 2017. As of the date of this report, the Postal Service has not been assessed any penalties associated with these non-payments.

As required by PAEA, OPM annually performs an actuarial valuation for the purpose of developing a payment schedule for the Postal Service to fund the remaining unfunded PSRHBF obligation in annual payments through the year 2056. Based on preliminary calculations provided by OPM, the Postal Service originally estimated that the amortization payment due September 30, 2018, would be $1.2 billion, and therefore accrued an expense of $595 million for the first six months of 2018. On July 19, 2018, the Postal Service received OPM's invoice for 2018, which indicated the year-end amortization payment amount due is $815 million. This amount was lower than the Postal Service's original estimate due to OPM's revision of certain inputs to the calculation. Due to the lower-than-estimated invoiced amount, the Postal Service has adjusted its accrual for the amortization payment, resulting in expenses of $16 million and $611 million for the three and nine months ended June 30, 2018, respectively. These amounts are included within *Retiree health benefits* in the accompanying unaudited *Statements of Operations*.

Furthermore, the Postal Service is obligated to pay the estimated normal costs of retiree health benefits attributable to the service of its employees during the most recently ended fiscal year. OPM's July 19, 2018, invoice indicated the normal cost payment amount due is $3.7 billion, and the Postal Service has recorded expenses of $884 million and $2.8 billion for the three and nine months ended June 30, 2018, respectively. These amounts are included within *Retiree health benefits* in the accompanying unaudited *Statements of Operations*.

The cumulative amount of PSRHBF statutorily-specified, normal cost and amortization payments the Postal Service has not made is $38.2 billion through September 30, 2017. As of June 30, 2018, the Postal Service has accrued an additional $3.4 billion for the 2018 amortization and normal cost payments due September 30, 2018. Given that OPM considers these amounts to be due and payable, the Postal Service reflects the cumulative unpaid amount as a current liability within *Retiree health benefits* in the accompanying *Balance Sheets*.

The following table details retiree health benefits expenses for the three and nine months ended June 30, 2018, and 2017:

	Three Months Ended June 30,		Nine Months Ended June 30,	
(in millions)	**2018**	**2017**	**2018**	**2017**
PSRHBF unfunded liability amortization expense[1]	$ 16	$ 332	$ 611	$ 716
Normal cost of retiree health benefits[2]	884	1,086	2,750	2,475
Total retiree health benefits expense	**$ 900**	**$ 1,418**	**$ 3,361**	**$ 3,191**

[1] Expense for the accrual for the annual payment due to PSRHBF by September 30 of the respective fiscal year, for the amortization of the unfunded liability. 2018 amounts are based on OPM's invoice received July 19, 2018, with updated discount rate assumptions. 2017 amounts include an adjustment to reflect an increase in the amount invoiced as compared to OPM's original estimate.

[2] Expense for the accrual for the annual payment due to the PSRHBF by September 30 of the respective fiscal year, for actuarially determined normal cost of retiree health benefits for current employees. 2018 amounts are based on OPM's invoice received July 19, 2018 resulting from revised actuarial assumptions. 2017 amounts include an adjustment to reflect the increase in the invoiced amount compared to OPM's original estimate.

NOTE 9 - WORKERS' COMPENSATION

Postal Service employees injured on the job are covered by the Federal Employees' Compensation Act ("FECA"), administered by the Department of Labor's ("DOL") Office of Workers' Compensation Programs, which makes all decisions regarding injured workers' eligibility for benefits. The Postal Service reimburses DOL for all workers' compensation benefits paid to or on behalf of Postal Service employees, plus an administrative fee.

Workers' Compensation Liability

The Postal Service records a liability for its workers' compensation obligations for employees who have been injured on the job and are eligible for benefits, or their qualified survivors. Both the current and noncurrent portions of the workers' compensation liability are recorded in the accompanying *Balance Sheets*. The Postal Service uses an estimation model that combines four generally-accepted actuarial valuation techniques based upon past claim-payment experience and exposure to claims as measured by total employee hours worked.

Changes in the liability are primarily attributable to the combined impacts of routine changes in actuarial assumptions, new compensation and medical cases, the progression of existing cases and changes in discount (interest) and inflation rates, including long-term cost-of-living-adjustment ("COLA") rates for compensation claims, and medical rates for medical claims. These rates are updated as of the balance sheet date and factored into the model in accordance with GAAP.

To determine the fair value of the liability each quarter, the Postal Service first estimates the future total cost of workers' compensation claims based on the dates of claim-related injuries, frequency or severity of the injuries, the pattern of historical payments to beneficiaries and the expected trend in future costs. The Postal Service then calculates the amount that would need to be invested at current discount (interest) rates to fully fund the future total cost of claims, and this calculated present value is the recorded value of the workers' compensation liability.

This liability calculation is highly sensitive to changes in discount rates. For example, a 1% increase in the discount rate would decrease the June 30, 2018, liability and related expense by approximately $1.7 billion. Likewise, a 1% decrease in the discount rate would increase the June 30, 2018, liability and related expense by approximately $2.1 billion.

The following table details the applicable discount rates for compensation and medical claims as of June 30, 2018, and September 30, 2017:

	June 30, 2018	**September 30, 2017**
Discount rates:		
Compensation claims	2.9%	2.5%
Medical claims	2.9%	2.5%

As of June 30, 2018, and September 30, 2017, the Postal Service's total liability for workers' compensation was approximately $16.6 billion and $17.9 billion, respectively. As of June 30, 2018, and September 30, 2017, the current portion of the liability was approximately $1.4 billion and $1.5 billion, respectively, and the noncurrent portion of the liability was approximately $15.2 billion and $16.4 billion, respectively, as reflected in the accompanying *Balance Sheets*.

Workers' Compensation Expense (Benefit)

The impacts of changes in discount rates and inflation rates, as well as the actuarial valuation of new cases and revaluation of existing cases, are components of total workers' compensation expense (benefit) as recorded in the accompanying unaudited *Statements of Operations*. In addition, the Postal Service pays an administrative fee to DOL, which is considered a component of workers' compensation expense.

The following table presents the components of workers' compensation expense (benefit) for the three and nine months ended June 30, 2018, and 2017:

	Three Months Ended June 30,		Nine Months Ended June 30,	
(in millions)	2018	2017	2018	2017
Impact of discount rate changes	$ (137)	$ 258	$ (694)	$ (1,346)
Actuarial revaluation of existing cases	49	(668)	(112)	(783)
Cost of new cases	275	361	920	1,202
Administrative fee	19	20	58	133
Total workers' compensation expense (benefit)	**$ 206**	**$ (29)**	**$ 172**	**$ (794)**

NOTE 10 - FAIR VALUE MEASUREMENT

The Postal Service defines fair value as the price that would be received upon sale of an asset or the price that would be paid to transfer a liability between unrelated parties.

The carrying amounts of certain current assets and liabilities, including cash, accounts receivable, accounts payable, accrued expenses and the current portion of debt, approximate fair value due to their short-term nature. Assets within *Property and equipment, net* are recorded at cost and measured at fair value on a nonrecurring basis if they are determined to be impaired or classified as assets held for sale.

Noncurrent receivables and noncurrent debt are measured using a fair value hierarchy model. This model prioritizes observable and unobservable inputs used to measure fair value, and consists of three broad levels, as defined in authoritative literature.

For the periods ended June 30, 2018, and September 30, 2017, no significant transfers between *Level 1* and *Level 2* assets or liabilities transpired. The carrying amount and fair value of the revenue forgone installment receivable and the noncurrent portion of debt are presented for disclosure purposes only in the following table:

	June 30, 2018		September 30, 2017	
(in millions)	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Revenue forgone installment receivable*	$ 441	$ 485	$ 426	$ 496
Noncurrent portion of debt	$ 2,200	$ 2,344	$ 4,900	$ 5,210

* The carrying amount is included within *Other assets* (which includes items in addition to the revenue forgone installment receivable) in the accompanying *Balance Sheets*.

The revenue forgone installment receivable qualifies as a financial instrument in accordance with authoritative literature. To calculate its fair value, the Postal Service recognizes the imputed interest it is owed as interest income and estimates the value of this receivable using the interest method, which converts future cash flows to a single discounted amount using interest rates for similar assets, which are considered *Level 2* inputs. The Postal Service then calculates the net present value of anticipated annual installment payments to be received, discounted by the 20-year U.S. Treasury Constant Maturity Rate, which was 2.91% and 2.63% as of June 30, 2018, and September 30, 2017, respectively.

The noncurrent portion of debt also qualifies as a financial instrument. Because no active market exists for the Postal Service's debt with the FFB, the fair value of the noncurrent portion of this liability has been estimated using expected future payments at risk-adjusted discount rates provided by the FFB, considered *Level 3* inputs.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

CAUTIONARY STATEMENTS

The following *Management's Discussion and Analysis of Financial Condition and Results of Operations* and other parts of this report describe the principal factors affecting the financial results, liquidity, capital resources and critical accounting estimates of the United States Postal Service ("Postal Service," "USPS," "we," "our" and "us"). Our results of operations may be impacted by risks and uncertainties discussed here and in our Annual Report on Form 10-K for the year ended September 30, 2017 ("Annual Report") filed with the Postal Regulatory Commission ("PRC") on November 14, 2017. Such factors, many of which we cannot control or influence, may cause actual results to differ materially from those currently contemplated.

Our operating results for the three and nine months ended June 30, 2018, are presented in accordance with accounting principles generally accepted in the United States ("GAAP"). These results are not necessarily indicative of the results to be expected for the year ended September 30, 2018, and should be read in conjunction with our Annual Report. All references to years in this report, unless otherwise stated, refer to fiscal years beginning October 1 and ending September 30. All references to quarters, unless otherwise stated, refer to quarters within fiscal years 2018 and 2017.

Forward-looking statements contained in this report represent our best estimates of known and anticipated trends believed relevant to future operations. However, actual results may differ significantly from current estimates. Certain forward-looking statements included in this report use such words as "may," "will," "could," "expect," "believe," "plan," "estimate," "project" or other similar terminology. These forward-looking statements, which involve a number of risks and uncertainties, reflect current expectations regarding future events and operating performance as of the date of this filing. We have no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

OVERVIEW

With our mandate to provide universal postal services to the nation, we serve retail and commercial customers in the U.S. as well as internationally. Our operations include an extensive and integrated retail, distribution, transportation and delivery network.

The *Postal Accountability and Enhancement Act* ("PAEA") classifies our products into two broad categories: Market-Dominant and Competitive "products," however, we use the term "services" in this document for consistency with other descriptions of services offered. The PAEA also established certain requirements that affect our financial results, including obligations for retirement benefits within the Civil Service Retirement System ("CSRS") and the Federal Employee Retirement System ("FERS"), and obligations for retiree health benefits including funding of the Postal Service Retiree Health Benefits Fund ("PSRHBF"). We must coordinate with the U.S. Office of Personnel Management ("OPM") to address these obligations.

We have successfully implemented initiatives that have reduced our costs by billions of dollars while offering new features for customers such as *Informed Delivery*. However, legal restrictions on pricing, service diversification and operations restrict our ability to fully implement our strategic objectives and cover our costs to provide prompt, reliable and efficient postal services to the nation.

We have established a core set of goals that drive our strategic initiatives and continuous improvement efforts:

1. Deliver a world-class customer experience;
2. Equip, empower and engage employees;
3. Innovate faster to deliver value; and
4. Invest in our future platforms.

As part of these efforts, we aim to achieve long-term financial stability, as well as a reduction in our debt. Our focus on maintaining liquidity and reducing operating expenses reflects current trends, as well as projected future volume of mail and packages. We believe that financial stability is within reach with targeted legislative and regulatory reform as we continue to identify and create innovative and affordable services, and deliver high levels of performance and service, and that such financial stability provides Congress and the Administration with additional time to address the broader public policy issues.

RESULTS OF OPERATIONS

SUMMARY

The major factors that impact our operating results include overall customer demand, the mix of postal services and contribution associated with those services, volume of mail and packages processed through our network and our ability to manage our cost structure in line with declining levels of mail volume, growth in more labor-intensive Shipping and Packages volume and an increasing number of delivery points. We operate as a single segment and report our performance as such.

Three Months Ended June 30, 2018

Operating revenue for the three months ended June 30, 2018, increased $409 million, or 2.5%, compared to the same period last year. Combined revenue from *First-Class Mail* and *Marketing Mail* decreased by $71 million, or 0.7%, for the period. *First-Class Mail* volume declined 499 million pieces for the period, while *Marketing Mail* volume increased 102 million pieces for the period due to increases in political and election mail from the mailings associated with the 2018 primary elections. Shipping and Packages revenue increased by $475 million, or 10.2%, as we continued to see growth in this lower-contribution business during the quarter.

Operating expenses for the three months ended June 30, 2018, decreased $240 million, or 1.3%, compared to the same period last year. Expenses for unfunded retirement and retiree health benefits declined by a combined $984 million during the quarter, however, this decline was due to adjustments recorded during the quarter and in the same period last year to account for revised actuarial assumptions. Partially offsetting this decline, compensation and benefits increased by $331 million due to additional hours incurred to support growth in the labor-intensive package business as well as contractual wage adjustments. In addition, workers' compensation expense increased by $235 million compared to the same period last year when we reduced our expense due to revised rules for pharmaceutical compounding. Furthermore, transportation expense grew by $142 million due to highway contract rate inflation as well as higher fuel costs, which other companies in the shipping business are also experiencing.

These changes in revenue and expenses resulted in a net loss of $1.5 billion for the three months ended June 30, 2018, compared to a net loss of $2.1 billion for the same period last year.

Nine Months Ended June 30, 2018

Operating revenue for the nine months ended June 30, 2018, increased $605 million, or 1.1%, compared to the same period last year. Combined revenue from *First-Class Mail* and *Marketing Mail* declined by $810 million, or 2.5%, for the period on a combined volume decline of nearly 3.1 billion pieces. Approximately 700 million pieces of this decline were due to the net decline in political and election mail volume for the nine months ended June 30, 2018, as volume associated with the 2018 primary elections was not enough to offset political and election mail volume from the same period last year, which included the 2016 general election season. These declines in *First-Class Mail* and *Marketing Mail* revenue were more than offset by the increase in Shipping and Packages revenue of over $1.4 billion, or 9.6%, as we continued to see growth in this lower-contribution business throughout the period.

Operating expenses for the nine months ended June 30, 2018, increased nearly $2.7 billion, or 5.0%, compared to the same period last year. Workers' compensation expense increased by $966 million as comparative changes in discount rates were smaller during the nine months ended June 30, 2018, than they were during the nine months ended June 30, 2017. Compensation and benefits increased by $630 million due largely to contractual wage adjustments and overtime hours. Unfunded retirement and retiree health benefits increased by a combined $522 million due to revised actuarial assumptions. Transportation expenses increased by $406 million due to highway contract rate inflation and increasing fuel costs, and other operating expenses increased by $205 million.

These changes in revenue and expenses resulted in a net loss of $3.4 billion for the nine months ended June 30, 2018, compared to a net loss of $1.3 billion for the same period last year.

Non-GAAP Controllable Loss

In the day-to-day operation of our business, we focus on costs over which we have some control, such as salaries and transportation. We calculate controllable loss, a non-GAAP measure, by excluding items over which we have no control, such as PSRHBF actuarial revaluation and amortization expenses, workers' compensation expenses caused by actuarial revaluation and discount rate changes, and retirement expenses caused by actuarial revaluation. Controllable loss should not be considered a substitute for net loss and other GAAP reporting measures.

The following table reconciles our GAAP net loss to controllable loss for the three and nine months ended June 30, 2018, and 2017:

(in millions)	Three Months Ended June 30, 2018	Three Months Ended June 30, 2017	Nine Months Ended June 30, 2018	Nine Months Ended June 30, 2017
Net loss	**$ (1,489)**	**$ (2,140)**	**$ (3,364)**	**$ (1,264)**
PSRHBF unfunded liability amortization expense[1]	16	332	611	716
Change in workers' compensation liability resulting from fluctuations in discount rates	(137)	258	(694)	(1,346)
Other change in workers' compensation liability[2]	(59)	(676)	(184)	(539)
CSRS unfunded liability amortization expense[3]	456	691	1,369	1,306
FERS unfunded liability amortization expense[4]	322	553	966	677
Change in normal cost of retiree health benefits due to revised actuarial assumptions[5]	2	395	104	395
Controllable loss	**$ (889)**	**$ (587)**	**$ (1,192)**	**$ (55)**

[1] Expense for the accrual for the annual payment due to PSRHBF by September 30 of the respective fiscal year, for the amortization of the unfunded liability. 2018 amounts are based on OPM's invoice received July 19, 2018, with updated discount rate assumptions. 2017 amounts include an adjustment to reflect an increase in the amount invoiced as compared to OPM's original estimate.

[2] Net amounts include changes in assumptions, as well as the valuation of new claims and revaluation of existing claims, less current year claim payments.

[3] Expense for the accrual for the annual payment due to OPM by September 30 of the respective fiscal year, to amortize the unfunded CSRS retirement obligation. 2018 amounts are based on updated Postal Service estimates resulting from revised actuarial assumptions. 2017 amounts include an adjustment to reflect an increase in the amount invoiced as compared to OPM's original estimate. Payments are to be made through 2043 based on OPM invoices.

[4] Expense for the accrual for the annual payment due to OPM by September 30 of the respective fiscal year, to amortize the unfunded FERS retirement obligation. 2018 amounts are based on updated Postal Service estimates resulting from revised actuarial assumptions. 2017 amounts include an adjustment to reflect an increase in the amount invoiced as compared to OPM's original estimate. Payments are to be made through 2047 based on OPM invoices.

[5] Represents the accrual for the portion or the increase in the annual normal cost payments due September 30, 2018, and 2017 attributable to revised actuarial assumptions and discount rate changes, based on OPM's invoices for the respective year. These amounts represent the noncontrollable portion of the expense recorded for normal cost of retiree health benefits.

Our controllable loss increased $302 million for the three months ended June 30, 2018, compared to the same period last year. This increase was largely driven by higher compensation and benefits expenses of $331 million, higher controllable portion (before adjustments for actuarial changes) of the normal cost of retiree health benefits expenses of $191 million, higher transportation expenses of $142 million and higher other operating expenses of $36 million, partially offset by the $409 million increase in operating revenue.

Our controllable loss increased over $1.1 billion for the nine months ended June 30, 2018, compared to the same period last year. This increase was largely driven by higher compensation and benefits expenses of $630 million, the higher controllable portion of the normal cost of retiree health benefits expenses of $566 million, higher transportation expenses of $406 million and higher other operating expenses of $205 million, partially offset by the $605 million increase in operating revenue.

These items are discussed in greater detail in *Operating Revenue and Volume* and *Operating Expenses*.

OPERATING REVENUE AND VOLUME

The combined categories of *First-Class Mail* and *Marketing Mail* continued to provide the majority of our revenue, despite long-term trends away from hard-copy communication to electronic media. Although this migration to electronic media has resulted in significant volume declines in *First-Class Mail* over the last decade, *Marketing Mail* volume had remained relatively steady since 2009, although *Marketing Mail* volume declined at a greater rate beginning in 2017 and continued to decline through the first half of 2018.

The following table summarizes our operating revenue and volume for the three and nine months ended June 30, 2018, and 2017, by each service line:

	Three Months Ended June 30,		Nine Months Ended June 30,	
(in millions)	**2018**	**2017**	**2018**	**2017**
Operating Revenue:				
First-Class Mail[1]	$ 5,919	$ 6,053	$ 19,061	$ 19,671
Marketing Mail[2]	3,983	3,920	12,420	12,620
Shipping and Packages[3]	5,151	4,676	16,220	14,795
International	630	659	2,205	2,068
Periodicals	341	347	984	1,049
Other[4]	1,050	1,010	2,832	2,914
Total operating revenue	**$ 17,074**	**$ 16,665**	**$ 53,722**	**$ 53,117**
Volume:				
First-Class Mail[1]	13,399	13,898	43,349	45,013
Marketing Mail[2]	18,550	18,448	58,202	59,591
Shipping and Packages[3]	1,465	1,363	4,641	4,359
International	205	252	741	781
Periodicals	1,357	1,363	3,860	4,048
Other[5]	93	108	254	286
Total volume	**35,069**	**35,432**	**111,047**	**114,078**

[1] Excludes *First-Class Package Service - Retail*.

[2] Excludes *Marketing Mail Parcels*.

[3] Includes *Priority Mail*, *USPS Retail Ground*, *Parcel Select Mail*, *Parcel Return Service Mail*, *Marketing Mail Parcels*, *Package Service Mail*, *First-Class Package Service - Retail*, *First-Class Package Service - Commercial* and *Priority Mail Express*.

[4] Revenue includes *PO Box services*, *Certified Mail*, Return Receipts, Insurance, Other Ancillary Services, Shipping and Mailing Supplies, Collect on Delivery, Registered Mail, Stamped Envelopes and Cards, money orders and Other services.

[5] Volume includes Postal Service internal mail and free mail provided to certain Congressionally-mandated groups.

For the three months ended June 30, 2018, *First-Class Mail* generated approximately 35% of operating revenue, a 1% decrease from the same period last year, and 38% of our volume, a 1% decrease from the same period last year. *Marketing Mail* generated approximately 23% of operating revenue and 53% of our volume, which were essentially unchanged compared to the same period last year.

For the nine months ended June 30, 2018, *First-Class Mail* generated approximately 35% of operating revenue, a 2% decrease from the same period last year, and approximately 39% of our volume, a 1% decrease from the same period last year. *Marketing Mail* generated approximately 23% of operating revenue and 52% of our volume, which were essentially unchanged compared to the same period last year.

We continued to experience strong results in our Shipping and Packages business, and it represented approximately 30% of our revenues for both the three and nine months ended June 30, 2018, which is a 2% increase from the same periods last year. Shipping and Packages generated 4% of our volume for both the three and nine months ended June 30, 2018, which was unchanged, compared to the same periods last year.

We implemented price increases of 0.9% and 1.9% on certain Market-Dominant services in January 2017 and January 2018, respectively. We also implemented price increases 3.9% and 4.1% on certain Competitive services in January 2017 and January 2018, respectively.

Our revenue growth is constrained by laws and regulations restricting the types of products, services and prices we can offer to our customers and the speed with which we can bring new products to market. *Marketing Mail* and our Shipping and

Packages business revenue and volume are closely linked to the strength of the U.S. economy and changes in how our customers use the mail; however, we have been active in pursuing growth opportunities.

To address the long-term trend that technological changes have had on our *First-Class Mail* revenue and volume, we have focused on providing new services, innovating with *Marketing Mail*, growing our e-commerce shipping business and implementing marketing campaigns that help us grow our Shipping and Packages business. By offering day-specific delivery, improved tracking and text alerts, and up to $50 of free insurance on most *Priority Mail* packages, we have demonstrated our responsiveness to our customers' needs.

First-Class Mail

First-Class Mail, presented in this report as a mail class and a Market-Dominant service category, includes cards, letters and flats. Prices of *First-Class Mail*, our most profitable service category, are the same regardless of how far the mail travels. Because *First-Class Mail* is classified by law as Market-Dominant, price increases are currently generally subject to a price cap based on the Consumer Price Index for All Urban Consumers ("CPI-U").

For the three months ended June 30, 2018, *First-Class Mail* revenue decreased $134 million, or 2.2%, and volume declined 499 million pieces, or 3.6%, compared to the same period last year. For the nine months ended June 30, 2018, *First-Class Mail* revenue decreased $610 million, or 3.1%, and volume declined 1.7 billion pieces, or 3.7%, compared to the same period last year. The most significant factor contributing to the declining trend in *First-Class Mail* volume was the continuing migration from mail to electronic communication and transaction alternatives.

Marketing Mail

USPS Marketing Mail (more commonly, *Marketing Mail*), presented as a mail class and a Market-Dominant service category, generally consists of advertising, newsletters, catalogs, small marketing parcels and other printed matter not required to be processed and delivered as *First-Class Mail* or *Periodicals.*

Marketing Mail has generally proven to be a relatively resilient marketing channel, and its value to U.S. businesses remains strong due to healthy customer returns on investment, and better data and technology integration. Between 2009 and 2016, *Marketing Mail* experienced relatively flat volume, although volume declined significantly in 2017 and continued to decline through the first half of 2018.

For the three months ended June 30, 2018, *Marketing Mail* revenue increased $63 million, or 1.6%, and volume grew by 102 million pieces, or 0.6%, compared to the same period last year. For the nine months ended June 30, 2018, *Marketing Mail* revenue decreased $200 million, or 1.6%, and volume declined by nearly 1.4 billion pieces, or 2.3%, compared to the same period last year. *Marketing Mail* revenue has been negatively impacted by the mail mix within various *Marketing Mail* services, as well as reductions in mail advertising campaigns by certain large mailers. *Marketing Mail* is also impacted by the volume of political and election mail with the mailings associated with periodic primary and general election seasons.

During the three months ended June 30, 2018, *Marketing Mail* was positively impacted by an increase in political and election mail compared to the same period last year, due to the mailings associated with the 2018 primary elections. For the three months ended June 30, 2018, the *Marketing Mail* portion of political and election mail produced approximately $98 million in revenue on volume of 471 million pieces, compared to approximately $18 million in revenue on volume of 93 million pieces for the same period last year.

During the nine months ended June 30, 2018, *Marketing Mail* was negatively impacted by a decline in political and election mail compared to the same period last year, a period that included the mailings associated with the 2016 general election. For the nine months ended June 30, 2018, the *Marketing Mail* portion of political and election mail produced approximately $176 million in revenue on volume of 864 million pieces, compared to $281 million in revenue on volume of nearly 1.6 billion pieces for the same period last year.

Marketing Mail is subject to intense competition, and price increases are generally capped at the rate of inflation. *Marketing Mail* volume is somewhat reflective of the cyclical nature of the U.S. economy, although targeted advertising campaigns can stimulate demand for this service, and our customers have used *Marketing Mail* to mail smarter and to more targeted prospects.

Shipping and Packages

The following table summarizes our operating revenue and volume for Shipping and Packages for the three and nine months ended June 30, 2018, and 2017, by each service:

(in millions)	Three Months Ended June 30, 2018	Three Months Ended June 30, 2017	Nine Months Ended June 30, 2018	Nine Months Ended June 30, 2017
Shipping and Packages Revenue:				
Priority Mail Services[1]	$ 2,402	$ 2,266	$ 7,708	$ 7,245
Parcel Services[2]	1,596	1,396	5,048	4,448
First-Class Package Services[3]	965	836	2,847	2,505
Package Services	188	178	617	597
Total Shipping and Packages revenue	**$ 5,151**	**$ 4,676**	**$ 16,220**	**$ 14,795**
Shipping and Packages Volume:				
Priority Mail Services[1]	266	259	845	821
Parcel Services[2]	738	684	2,376	2,205
First-Class Package Services[3]	316	286	939	869
Package Services	145	134	481	464
Total Shipping and Packages volume	**1,465**	**1,363**	**4,641**	**4,359**

[1] Includes *Priority Mail*, a 1-3 business day delivery service; *Priority Mail Express*, an overnight delivery service available 365 days per year; and *USPS Retail Ground,* a retail-only Market-Dominant service priced identically and functionally equivalent to *Priority Mail* for Zones 1-4.

[2] Includes *Parcel Select*, *Parcel Return*, and *Marketing Mail Parcels*.

[3] Includes *First-Class Package Services - Retail* and *First-Class Package Services - Commercial*.

Our Shipping and Packages business has continued to show solid revenue and volume growth as a result of our successful efforts to compete in shipping services, including "last-mile" e-commerce fulfillment markets and Sunday delivery as well as end-to-end markets, although the rate of growth is slowing. Volume growth has been driven by consumers' continued use of online shopping, which provided a surge in package volume with a record number of packages delivered during both the calendar year 2016 and 2017 holiday seasons. To accommodate this surge in volume and to avoid service disruptions during the peak holiday seasons, we increased Sunday delivery service for some of our customers in limited U.S. markets and added non-career employees for the peak seasons in accordance with our labor agreements.

Priority Mail Services

Priority Mail Services, our Shipping and Packages subcategory that includes *Priority Mail*, *Priority Mail Express* and *Retail Ground*, allows customers the ability to send documents and packages requiring expedited transportation and handling. While Priority Mail Services revenue continues to grow year over year, its service offerings are somewhat price sensitive, particularly with retail customers, and its growth rate has slowed down and is lower than other Shipping and Packages subcategories used by commercial customers.

Priority Mail Services accounts for our largest portion of Shipping and Packages revenue, representing approximately 47% and 48% of the total for the three and nine months ended June 30, 2018, respectively, compared to 49% for each of the same periods last year.

For the three months ended June 30, 2018, Priority Mail Services revenue grew by 6.0% on volume growth of 2.7%, compared to the same period last year. For the nine months ended June 30, 2018, Priority Mail Services revenue grew by 6.4% on volume growth of 2.9%, compared to the same period last year. Revenue grew more than volume for the periods due to the January 2017 and January 2018 price increases applicable to Competitive services.

Parcel Services

Our Parcel Services subcategory includes Competitive services *Parcel Select* and *Parcel Return* as well as Market-Dominant *USPS Marketing Mail Parcels* (more commonly, *Marketing Mail Parcels*). Parcel Services largely consist of "last-mile" deliveries, offered to large bulk shippers that drop parcels deeper into our network.

For the three months ended June 30, 2018, revenue from Parcel Services increased by 14.3% compared to the same period last year. For the nine months ended June 30, 2018, revenue from Parcel Services increased by 13.5% compared to the same period last year. This subcategory showed strong volume growth of 7.9% and 7.8%, respectively, over the same periods last year, driven largely by the continuing growth of e-commerce. However, this subcategory is primarily a "last-mile" service that bypasses much of our infrastructure and therefore is one of our lowest-priced package services, and as a result, produces a lower yield per piece when compared to many of our other services. Revenue grew more than volume for the periods due to the January 2017 and January 2018 price increases applicable to Competitive services.

First-Class Package Services

The First-Class Package Services subcategory includes the competitively priced *First-Class Package Service - Retail*, a Competitive service for under-13-ounce packages targeted to retail customers, and *First-Class Package Service - Commercial*, an under-one-pound Competitive service targeted to commercial customers. This subcategory offers customers that ship primarily lightweight fulfillment parcels the lowest-priced expedited end-to-end tracked package option in the marketplace. First-Class Package Services revenue and volume performance has experienced strong increases for the past several years, primarily attributable to growth in e-commerce.

For the three months ended June 30, 2018, First-Class Package Services revenue increased 15.4% on volume growth of 10.5%, compared to the same period last year. For the nine months ended June 30, 2018, First-Class Package Services revenue increased 13.7% on volume growth of 8.1%, compared to the same period last year. Revenue grew more than volume for the periods due to the January 2017 and January 2018 price increases applicable to Competitive services.

Package Services

Customers use our Package Services subcategory for shipping merchandise or bound printed matter, including library and media mail, weighing up to 70 pounds. For the three months ended June 30, 2018, Package Services revenue increased 5.6% on volume growth of 8.2%, compared to the same period last year. For the nine months ended June 30, 2018, Package Services revenue increased 3.4% on volume growth of 3.7%, compared to the same period last year. Revenue growth in this category has generally not kept up with volume growth due to price caps and bulk rates offered to certain high-volume shippers of bound printed matter parcels.

International Mail

Our International Mail category includes several services that enable customers, both domestic and abroad, to send international mail, including postcards, envelopes, flats and packages with either standard or express delivery options. "Outbound" services, which allow customers in the U.S. to send mail and packages to other countries, generate approximately two thirds of International Mail revenue, but "inbound" services are the opposite, generating two thirds of volume but only a third of the revenue. This is primarily due to the lower rates for inbound international e-commerce packages.

For the three months ended June 30, 2018, International Mail revenue decreased 4.4% on a volume decline of 18.7%, compared to the same period last year. For the nine months ended June 30, 2018, International Mail revenue increased 6.6% on a volume decline of 5.1%, compared to the same period last year. The decrease in revenue for the three-month period is largely correlated to the inbound volume decline, whereas the increase in revenue for the nine-month period is largely the result of higher rates resulting from the January 2017 and January 2018 price increases and new bilateral agreements.

Periodicals

Periodicals, also presented as a mail class and a Market-Dominant service category, is designed for newspapers, magazines and other periodical publications whose primary purpose is transmitting information to an established list of subscribers or requesters. For the three months ended June 30, 2018, *Periodicals* revenue decreased by 1.7% and volume declined by 0.4%, compared to the same period last year. For the nine months ended June 30, 2018, *Periodicals* revenue decreased by 6.2% and volume declined by 4.6%, compared to the same period last year.

Periodicals revenues and volumes have been in decline for more than a decade as trends in hard-copy reading behavior and shifts of advertising away from print have depressed this business. The *Periodicals* category is not expected to rebound as electronic content continues to grow in popularity with the public.

Other

Other services include ancillary services such as *Certified Mail*, *PO Box* services, and *Return Receipt* services. Also included in this category are money orders and passport services. Other services revenue increased by 4.0% for the three months ended June 30, 2018, and decreased by 2.8% for the nine months ended June 30, 2018, compared to the same periods last year.

OPERATING EXPENSES

In an effort to align our resources with anticipated future mail and package volume, we continue to aggressively manage operating expenditures under management's control.

Our mail processing and distribution network was designed to provide overnight delivery service of *First-Class Mail* within specified delivery areas for a much higher volume of mail than we are required to process and deliver today, and the network's legacy capabilities are not completely aligned to today's mail mix and volumes. Consequently, certain of our processing and distribution facilities continue to operate at less than full capacity. Our challenge to contain costs is also compounded by the increasing number of delivery points, which, when combined with lower hard-copy mail volume, has resulted in a drop in the average number of pieces delivered per delivery point per day from approximately 5.5 pieces in 2007 to 3.6 pieces in 2017, a reduction of approximately 35%.

Compensation and Benefits

Compensation and benefits is our largest operating expense category. These expenses consist of costs related to our active career and non-career employees. Overall, our compensation and benefits expenses increased 2.7% and 1.7% for the three and nine months ended June 30, 2018, respectively, compared to the same periods last year.

The following table presents compensation and benefits expenses for the three and nine months ended June 30, 2018, and 2017:

	Three Months Ended June 30,		Nine Months Ended June 30,	
(in millions)	**2018**	**2017**	**2018**	**2017**
Compensation	$ 9,300	$ 9,003	$ 28,551	$ 28,014
FERS employees' current year service	1,666	1,630	5,037	4,951
Employee health benefits	1,297	1,295	3,887	3,865
Other	80	84	238	253
Total compensation and benefits	**$ 12,343**	**$ 12,012**	**$ 37,713**	**$ 37,083**

Compensation

Compensation expense increased 3.3% and 1.9% for the three and nine months ended June 30, 2018, respectively, compared to the same periods last year. These increases for both the three and nine months ended June 30, 2018, were primarily due to contractual wage adjustments and overtime hours, compared to the same periods last year.

For the three months ended June 30, 2018, total work hours were approximately 289 million, which was an increase of 1.4%, compared to the 285 million total work hours for the three months ended June 30, 2017. For the nine months ended June 30, 2018, total work hours were approximately 882 million, which was an increase of 0.1%, compared to the 881 million total work hours for the nine months ended June 30, 2017. These increases are the result of supporting continuous volume growth in our labor-intensive Shipping and Packages business.

The number of career employees decreased by approximately 14,000, or 2.9%, at June 30, 2018, compared to the same date a year ago. The decrease in the number of career employees primarily reflects normal attrition as we continue to align our workforce with declining mail volume.

The number of non-career employees increased by approximately 2,200, or 1.7%, at June 30, 2018, compared to the same date a year ago. The additional use of both non-career employees and employees newly converted from non-career to career at a lower wage structure mitigates some of the upward wage and benefit pressures for career employees, and helps to constrain costs.

In May 2018, we agreed to extend contract negotiations on a new collective bargaining agreement with the National Rural Letter Carriers' Association ("NRLCA"). Our contract with the NRLCA expired on May 20, 2018, and the respective parties mutually agreed to extend negotiations beyond the deadline.

FERS Employees' Current Year Service

The majority of our career employees participate in either CSRS or FERS based on the starting date of their employment with us or another U.S. government employer. We incur normal costs for FERS employees; however, by law we do not pay normal costs for CSRS retirement benefits. Career employees may also participate in the Thrift Savings Plan ("TSP"), a defined contribution retirement savings and investment plan administered by the Federal Retirement Thrift Investment Board. Our TSP expenses are related only to our contributions for FERS employees who participate in the TSP.

Our expense for FERS employees' current year service consists of FERS normal cost, Social Security and employer TSP contributions, and is reported within *Compensation and benefits* under *Operating expenses* in the accompanying unaudited *Statements of Operations*. We record our contributions to FERS, Social Security and TSP as an expense in the period during which the contribution is incurred. We recognize the expense for each period's legally required contribution, and record a liability for any contribution due and unpaid at the end of each reporting period. The cost of unfunded FERS retirement benefits is reported separately within *Unfunded retirement benefits* in the accompanying *Balance Sheets*, as discussed below. For additional information, see below and see *Item 1. Financial Statements, Notes to Unaudited Financial Statements, Note 7 - Retirement Plans*.

The following table presents the details of FERS employees' current year service expenses for the three and nine months ended June 30, 2018, and 2017:

	Three Months Ended June 30,		**Nine Months Ended June 30,**	
(in millions)	**2018**	**2017**	**2018**	**2017**
FERS normal costs	$ 871	$ 868	$ 2,609	$ 2,603
Social Security	519	491	1,599	1,536
TSP	276	271	829	812
Total FERS employees' current year service	**$ 1,666**	**$ 1,630**	**$ 5,037**	**$ 4,951**

FERS employees' current year service expenses increased 2.2% and 1.7% for the three and nine months ended June 30, 2018, respectively, compared to the same periods last year, driven by increases to Social Security contributions.

Our FERS normal cost contribution rate remained steady at 13.7% of basic pay for most participants during both 2018 and 2017. Expenses for the FERS normal costs, Social Security and employer TSP contributions remained relatively unchanged for both the three and nine months ended June 30, 2018, compared to the same periods last year. This is consistent with the general trends in the number of career employees during the comparable periods. As most of our employees participate in FERS, this was also consistent with the trends in compensation for the period, described above in *Compensation*.

Employee Health Benefits

Our expense for employee health benefits is most significantly impacted by the number of employees electing coverage and the premium costs of the selected plans. Our active employees may participate in the Federal Employees Health Benefits ("FEHB") Program, which is administered by OPM. We account for employee benefit costs as an expense in the period in which our contributions to the plans under the program are due.

Employee health benefits expense increased 0.1% and 0.6% for the three and nine months ended June 30, 2018, respectively, compared to the same periods last year, primarily due to an increase in premiums for the 2018 calendar year. On average, healthcare premiums rose 4.0% for the 2018 calendar plan year, while the average increase in our premium contributions is approximately 1.5%. This premium increase affected the three and nine months ended June 30, 2018, although this increase was partially offset by the lower contribution rate of the employer portion of healthcare premiums that we paid and the reduction in number of career employees, as previously discussed.

Our share of healthcare premiums for our employees represented 72.5% and 73.6% of the total healthcare premium costs for the three months ended June 30, 2018, and 2017, respectively. Our share of healthcare premiums for our employees represented 72.9% and 73.8% of the total healthcare premium costs for the nine months ended June 30, 2018, and 2017, respectively. These decreases in our share of healthcare premium costs for employees were consistent with the terms of our contractual agreements; however, these decreases were offset by overall rising premium costs.

CSRS and FERS Unfunded Retirement Benefits Amortization

OPM periodically notifies us regarding its revaluation of unfunded CSRS and FERS retirement benefits. Prior to 2018, OPM calculated these obligations using government-wide economic and demographic data, rather than Postal Service-specific demographics and economic assumptions. The amounts we record for the expenses for our unfunded CSRS and FERS liabilities may be significantly impacted by changes in actuarial assumptions used to revalue the unfunded liabilities.

During the third quarter of 2017, we recorded adjustments to our CSRS and FERS amortization expenses due to revised actuarial assumptions. In June of 2017, we received an invoice from OPM in the amount of $1.7 billion for the first annual CSRS amortization payment due September 30, 2017. We therefore recorded an additional $383 million accrual for the CSRS amortization expense for the three and nine months ended June 30, 2017, to adjust for the increase in the invoiced amount compared to the previous estimate. Furthermore, we revised our estimate of our FERS annual amortization payment due September 30, 2017, to $903 million, based on preliminary discussions with OPM regarding its updated actuarial assumptions. This adjustment resulted in an increase in our FERS amortization expense of $491 million for both the three and nine months ended June 30, 2017.

In October 2017, OPM issued a new rule announcing its intent to calculate future unfunded CSRS and FERS obligations using Postal Service-specific demographic assumptions. The new rule did not fully address our concerns, given that it did not address the use of government-wide versus Postal Service-specific economic assumptions.

Also in October 2017, OPM provided an actuarial report indicating that the projected amortization payments due to OPM by September 30, 2018, will be $1.7 billion for CSRS unfunded retirement benefits and $917 million for FERS unfunded retirement benefits. These projected payments did not include the estimated effect of the above-discussed transition to Postal Service-specific demographic assumptions.

In April 2018, the Board of Actuaries of the CSRS, which oversees OPM's calculation of actuarial liabilities for CSRS and FERS, lowered the discount rate used to calculate CSRS and FERS unfunded retirement liabilities from 4.5% to 4.25%. Assuming the use of Postal Service-specific demographic assumptions, we estimate that this change in discount rate will increase the projected amortization payment due to OPM by September 30, 2018, for CSRS unfunded retirement benefits to approximately $1.8 billion for FERS unfunded retirement benefits to approximately $1.3 billion.

Accordingly, we have accrued $456 million and $1.4 billion for the three and nine months ended June 30, 2018, respectively, for the CSRS amortization expense. Likewise, we have accrued $322 million and $966 million for the three and nine months ended June 30, 2018, respectively, for the FERS amortization expense. Although our estimated year end payment obligations for both CSRS and FERS increased in 2018 from the invoiced amounts in 2017, our amortization expenses for the three months ended June 30, 2018, declined compared to three months ended June 30, 2017, due to the adjustments we made in that period resulting from changes in actuarial assumptions.

We expect to receive invoices from OPM for the actual amounts due for CSRS and FERS during the fourth quarter of 2018, and the amounts invoiced could differ from the projected amounts, due to changes in discount rates, actuarial assumptions and experience as of the calculation date.

For additional information, see *Item 1. Financial Statements, Notes to Unaudited Financial Statements, Note 7 - Retirement Plans*.

Retiree Health Benefits

We participate in federal employee benefit programs for retiree health benefits. Retirees who participated in FEHB for the five years immediately preceding their retirement may continue to participate in the plan during retirement. Qualifying survivors of retirees are also eligible to receive benefits.

In accordance with PAEA, since the beginning of 2017, the PSRHBF has been used to fund our share of retiree health benefit premiums. Also since 2017, we have been obligated to pay into the PSRHBF the actuarially determined normal costs of retiree health benefits attributable to the service of our employees, as well as the amortization payment for the PSRHBF unfunded liability. Our total retiree health benefits expense therefore consists of both the normal and the amortization costs. For these, we record contributions to the plans as an expense in the period in which each contribution is due.

The PAEA required us to prefund retiree health benefits during years 2007 through 2016 by paying annual amounts ranging from $1.4 billion to $5.8 billion, totaling $54.8 billion, into the PSRHBF, which began paying our share of retiree health benefit premiums in 2017. We remain obligated to fund the $33.9 billion in PSRHBF prefunding payments that we defaulted on for the years 2012 through 2016, as well as the amortization and normal cost payments of $955 million and $3.3 billion, respectively, which we did not pay in 2017. As of the date of this report, we have not been assessed any penalties associated with these non-payments.

As required by PAEA, OPM annually performs an actuarial valuation for the purpose of developing a payment schedule for us to fund the remaining unfunded PSRHBF obligation in annual payments through the year 2056. Based on preliminary calculations provided by OPM, we originally estimated that the amortization payment due September 30, 2018, would be $1.2 billion, and therefore accrued an expense of $595 million for the first six months of 2018. On July 19, 2018, we received OPM's invoice for 2018, which indicated the year-end amortization payment amount due is $815 million. This amount was lower than our original estimate due to OPM's revision of certain inputs to the calculation. Due to the lower-than-estimated invoiced amount, we have adjusted our accrual for the amortization payment, resulting in expenses of $16 million and $611 million for the three and nine months ended June 30, 2018, respectively.

Furthermore, we are obligated to pay the estimated normal costs of retiree health benefits attributable to the service of our employees during the most recently ended fiscal year. OPM's July 19, 2018 invoice indicated the normal cost payment amount due is $3.7 billion, and we have recorded expenses of $884 million and $2.8 billion for the three and nine months ended June 30, 2018, respectively.

For the three months ended June 30, 2018, our total retiree health benefits expense decreased by $518 million, or 36.5%, compared to the same period last year. For the nine months ended June 30, 2018, our retiree health benefits expense increased by $170 million, or 5.3%, compared to the same period last year. The amounts we accrued during the third quarter of 2017 included adjustments to reflect increases in the amounts invoiced by OPM in July of 2017 compared to its original 2017 estimate. This caused retiree health expenses to be higher for both the three and nine months ended June 30, 2017, than what they otherwise would have been, which affected the year-over-year comparisons.

For additional information, see *Item 1. Financial Statements*, *Notes to Unaudited Financial Statements*, *Note 8 - Health Benefits Plans*, *Retirees.*

Workers' Compensation

Our employees injured on the job are covered by the Federal Employees' Compensation Act ("FECA"), administered by the Department of Labor's ("DOL") Office of Workers' Compensation Programs, which makes all decisions regarding injured workers' eligibility for benefits. We are legally mandated to participate in the federal workers' compensation program. Our workers' compensation (benefit) expense reflects the impacts of changes in discount rates, as well as the actuarial valuation of new workers' compensation cases and revaluation of existing ones. We reimburse the DOL for all workers' compensation benefits paid to or on behalf of our employees, plus an administrative fee.

The following table presents the components of workers' compensation expense (benefit), including the cash payments made by DOL on behalf of workers' compensation obligations, for the three and nine months ended June 30, 2018, and 2017:

(in millions)	**Three Months Ended June 30, 2018**	**Three Months Ended June 30, 2017**	**Nine Months Ended June 30, 2018**	**Nine Months Ended June 30, 2017**
Impact of discount rate changes	$ (137)	$ 258	$ (694)	$ (1,346)
Actuarial revaluation of existing cases	49	(668)	(112)	(783)
Cost of new cases	275	361	920	1,202
Administrative fee	19	20	58	133
Total workers' compensation expense (benefit)	**$ 206**	**$ (29)**	**$ 172**	**$ (794)**
Less: cash payments made by DOL on behalf of workers' compensation obligations	402	389	1,050	1,091
Total non-cash workers' compensation (benefit)	**$ (196)**	**$ (418)**	**$ (878)**	**$ (1,885)**

For the three months ended June 30, 2018, the portion of workers' compensation expense due to the impact of discount rate changes decreased $395 million, compared to the same period last year. For the nine months ended June 30, 2018, the portion of workers' compensation expense due to the impact of discount rate changes increased $652 million, compared to the same period last year. These changes are the result of changes in interest rates, outside of management's control.

The combined costs of new workers' compensation cases and revaluation of existing workers' compensation cases have increased by $631 million and $389 million for the three and nine months ended June 30, 2018, respectively, compared to the same periods last year. These increases are largely driven by the impact of actuarial revaluation of existing cases during 2017 as a result of the positive changes that DOL implemented in the rules associated with prescriptions for compound pharmaceuticals during that year. Changes in actuarial valuation are primarily attributable to the combined impacts of routine changes in actuarial estimation, the progression of existing cases and updated cost-of-living-adjustment ("COLA") assumptions, which are largely outside of management's control.

Under FECA, workers' compensation claims for many types of injuries cannot be settled through lump-sum payments, and in some instances with regard to those claims, compensation may be paid over many years. Federal law grants COLA rates to those claims, and these factors result in substantially higher costs to us than would likely result if we managed our own claims. Additionally, since we do not manage the FECA program, we have no ability to control the significant administrative costs associated with managing the claims and payments process.

For additional information, see *Item 1. Financial Statements*, *Notes to Unaudited Financial Statements*, *Note 9 - Workers' Compensation*.

Transportation

Transportation expense includes the costs we incur to transport mail and other products between our facilities, comprising of highway, air and international transportation contracts, plus contract delivery services.

With the exception of contract delivery services, our costs to deliver mail and other products to delivery points are not included within *Transportation* but in *Compensation and benefits* for employee costs and in *Other operating expenses* for fuel, vehicle maintenance and repair, and other costs. Furthermore, transportation expense does not include the compensation of employees responsible for transporting mail and other products between our facilities.

Variations in the volume and weight of mail transported and the mode of transportation used have significant impact on transportation expenses. The components of transportation expense for the three and nine months ended June 30, 2018, and 2017, are presented in the following table:

	Three Months Ended June 30,		Nine Months Ended June 30,	
(in millions)	2018	2017	2018	2017
Highway	$ 1,037	$ 968	$ 3,258	$ 3,094
Air	693	608	2,178	1,916
International	142	150	475	480
Other	10	14	29	44
Total transportation expenses	**$ 1,882**	**$ 1,740**	**$ 5,940**	**$ 5,534**

Overall, transportation expenses increased 8.2% and 7.3% for the three and nine months ended June 30, 2018, respectively, compared to the same periods last year.

Highway transportation expenses increased 7.1% and 5.3% during the three and nine months ended June 30, 2018, respectively, compared to the same periods in the prior year. These increases were due primarily to higher diesel fuel prices and higher unit costs per mile due to supplier cost pressures resulting in part from a national shortage of truck drivers.

Air transportation expenses increased 14.0% and 13.7% during the three and nine months ended June 30, 2018, respectively, compared to the same periods in the prior year. These increases were due primarily to increased package volume, higher jet fuel prices and increased spend on charters.

International transportation expenses are related only to outbound services that allow customers in the U.S. to send mail and packages to other countries. For the three and nine months ended June 30, 2018, international transportation expenses decreased 5.3% and 1.0%, respectively, primarily due to a decrease in our international service volumes.

Other Operating Expenses

Other operating expenses for the three and nine months ended June 30, 2018, and 2017, are detailed in the following table:

	Three Months Ended June 30,		Nine Months Ended June 30,	
(in millions)	2018	2017	2018	2017
Supplies and services	$ 716	$ 737	$ 2,243	$ 2,234
Depreciation and amortization	421	431	1,247	1,256
Rent and utilities	384	376	1,271	1,191
Information technology and communications	238	230	659	653
Vehicle maintenance service	164	159	477	481
Rural carrier equipment maintenance	138	127	406	375
Fuel - delivery vehicles	125	101	375	311
Miscellaneous other	241	230	809	781
Total other operating expenses	**$ 2,427**	**$ 2,391**	**$ 7,487**	**$ 7,282**

Aside from a 23.8% and 20.6% increases for fuel associated with our delivery vehicles that were driven by both higher unleaded gas prices and increased usage due to package volume growth, compared to the same periods in the prior year, the period-over-period changes in other operating expenses for the three and nine months ended June 30, 2018, were relatively immaterial, increasing overall by 1.5% and 2.8%, respectively, compared to the same periods in the prior year.

LIQUIDITY AND CAPITAL RESOURCES

We held unrestricted cash and cash equivalents of $11.2 billion and $10.5 billion as of June 30, 2018, and September 30, 2017, respectively. Our average daily liquidity balance during the nine months ended June 30, 2018, was $11.2 billion, representing approximately 37 days of liquidity available, which we define as unrestricted cash plus available borrowing capacity divided by estimated average cash disbursements (including capital expenditures) per business day (usually 251 cash disbursement days per year).

CASH FLOW ANALYSIS

Although our cash balances have increased since 2012, they remain insufficient to support an organization with approximately $72 billion in annual operating expenses. More significantly, this increase would not have occurred at all had we not been forced to default on $33.9 billion in legally-obligated PSRHBF prefunding payments. We also did not make payments due to OPM by September 30, 2017, totaling $6.9 billion, which included amortization payments for CSRS, FERS and PSRHBF unfunded liabilities, and the normal cost of retiree health benefits. We did not make these payments (and previously defaulted on the statutorily fixed PSRHBF payments) in order to preserve liquidity to ensure that our ability to fulfill our primary universal service mission was not placed at undue risk.

Looking forward, our operations will require significant capital investment over the next few years to modernize and improve our processing and delivery infrastructure in order to be able to continue to meet our statutory obligation to provide prompt, reliable, and efficient postal services to the nation. Furthermore, given our inability to raise cash through the issuance of additional debt, our current level of available liquidity may be insufficient to support our operations in the event of another significant downturn in the U.S. economy.

Operating Activities

Cash provided by operating activities decreased by $907 million, or 35.8%, for the nine months ended June 30, 2018, compared to the same period last year. This decrease is primarily the result of higher cash expenditures for compensation and benefits and transportation, along with an increase in receivables, partially offset by the increase in revenue.

Price Increases

The following table reflects our recent price increases along with the service category, date the notice was filed with the PRC, effective date of the increase, increase percentage, and the estimated annual revenue expected to be generated by the respective increase.

Service Category	Date Notice Filed with PRC	Effective Date of Increase	Increase %	Estimated Annual Revenue *($ in millions)*
Market-Dominant	October 12, 2016	January 22, 2017	0.9%	$ 360
Competitive	October 19, 2016	January 22, 2017	3.9%	507
Competitive*	July 26, 2017	September 3, 2017	9.9%	—
Market-Dominant	October 6, 2017	January 21, 2018	1.9%	655
Competitive	October 6, 2017	January 21, 2018	4.1%	356

* Represents a transfer of *First-Class Package Service - Retail* (formerly *First-Class Mail Parcels*) from a Market-Dominant service to a Competitive service, along with an average price increase of 9.9% on that service. The estimated impact to annual revenue is immaterial as the annual volume for this service is low.

Investing Activities

We invested $905 million in the purchase of property and equipment for the nine months ended June 30, 2018, which is a decrease of $92 million, or 9.2%, compared to the same period last year. This decrease is principally related to the timing of our capital investment purchases; however, the current amount of our projected capital expenditures is approximately $1.3 billion for 2018.

Financing Activities

Except as described otherwise in this quarterly report, the nature and amounts of our payment obligations under our debt, capital and operating lease agreements, purchase commitments and other liabilities as of June 30, 2018, have not materially changed from those described in our Annual Report.

On September 30, 2012, we reported that we had reached the maximum borrowing amount allowed under our statutory debt ceiling, and the amount of debt we have reported each quarter has not changed since then. Our debt is borrowed from the Federal Financing Bank ("FFB"), a government-owned corporation under the general supervision of the Secretary of the Treasury, and consists of fixed-rate notes and two revolving credit facilities with various maturities with an aggregate principal balance of $15.0 billion as of June 30, 2018, and September 30, 2017.

The two revolving credit facilities have interest rates determined by the U.S. Department of the Treasury each business day and enable us to draw up to $4.0 billion in total. As of June 30, 2018, and September 30, 2017, these facilities were fully drawn and were included in the current portion of debt. These annually-renewable facilities were renewed on April 20, 2018, and are scheduled to expire and be renewed in April 2019.

LIQUIDITY OUTLOOK

With the anticipated continued migration to electronic communication and transactional alternatives, we continue to pursue long-term financial sustainability by focusing on the following items:

1. Continued efforts to control costs and drive efficiencies, innovate to keep mail relevant and generate increased revenue;
2. Postal Service reform legislation that includes the following terms:
    a. Allowing us to adopt Postal Service-specific economic and demographic assumptions for calculating pension liabilities,
    b. Establishing a set of healthcare plans within the FEHB that would fully integrate with Medicare for current and future retirees, which we believe would improve the affordability of our retiree health benefits system and eliminate most of the unfunded PSRHBF obligations, and
    c. Restoring half of the exigent surcharge (the 4.3% surcharge on Market-Dominant services that was effective from January 2014 to April 2016), as a permanent part of our rate base; and
3. Favorable outcome of the PRC's ten-year review (discussed below), which would allow additional pricing flexibility.

Although we continue to inform the Administration, Congress, the PRC and other stakeholders of the immediate and long-term financial challenges we face, we have no assurances that our requests will result in meaningful reform in the foreseeable future.

PRC Ten-year Review

On December 1, 2017, the PRC announced its initial decision in connection with its ten-year review of the system for regulating rates and classes for Market-Dominant products as required by the PAEA. The purpose of the ten-year review was to determine if the system for regulating rates and classes has achieved the objectives established by Congress in the PAEA. As part of this review, the PRC evaluated the CPI-U price cap for our Market-Dominant services.

The PRC concluded that the rates system has not achieved its necessary objectives and needs to be changed, because it does not enable us to achieve our mission of providing prompt, reliable, and efficient universal postal services to the American people in a financially sustainable manner. The PRC's proposed changes to the system do not include the elimination of the CPI-U price cap; however, its proposal does provide for some additional pricing authority within a price cap system. The Postal Service continues to assert that the price cap should be eliminated and that the PRC should engage in "after-the-fact," "light-touch" review of the Market-Dominant prices set by the Postal Service to ensure that those prices are just and reasonable.

The PRC will issue a final rule after considering the comments and reply comments of any interested stakeholders, which were due no later than March 1, 2018, and March 30, 2018, respectively. Additional information regarding the ten-year review may be found at the PRC website: https://www.prc.gov/press-releases/prc-concludes-rate-system-has-not-achieved-necessary-objectives-and-issues-proposed.

2018 and Beyond

We anticipate that given our ongoing liquidity concerns, and without legislative action and regulatory reform, we may not be able to pay all legally-required obligations and also invest in much-needed capital expenditures in 2018 and future years that are necessary to ensure our ability to fulfill our primary mission. Furthermore, we believe that continuing productivity improvements alone will not be sufficient to address the challenges presented by declining Market-Dominant volume and revenue, and that growth in operating revenue will unlikely be able to keep pace with increased costs.

Legally-Required Obligations
In addition to our previously discussed obligations for unfunded retirement and retiree health benefits of approximately $7.6 billion due on September 30, 2018, we expect to pay the DOL approximately $1.4 billion in October 2018, representing the workers' compensation claims paid by DOL for the chargeback year July 1, 2017, to June 30, 2018, plus the estimated administrative fee.

Capital Investments
We currently estimate that our required cash outlays for necessary and overdue capital investments necessary to ensure that we can perform our universal service obligation will amount to approximately $400 million for the remainder of 2018, and an additional $9.4 billion for years 2019 through 2022, as we plan to invest in a new fleet of delivery vehicles and other capital expenditures. Although our future projections include these capital cash outlays, future cash flow from operations alone may not generate the cash needed to enable us to fully fund such necessary capital investments.

Mitigating Circumstances
We continue to pursue strategies within our control to increase operational efficiency and improve liquidity. We have conserved capital in recent years by spending only what we believed was essential to maintain our existing facilities and service levels and to increase efficiencies. However, an increase in capital investment is necessary to upgrade our facilities, fleet of vehicles and processing equipment in order to remain operationally viable.

We continue to support legislation that will enable us to increase revenue and reduce costs. Specifically, current proposed legislation would establish a set of health care plans within FEHB fully integrated with Medicare for our current and future retirees, eliminate most of the current retiree health benefits unfunded liability, require Postal Service-specific demographic and economic assumptions in calculating pension liabilities, substantially reduce annual amortization and normal cost payment requirements, reinstate half of the exigent surcharge and authorize the provision of non-postal services to state, local and tribal governments.

Our status as an independent establishment of the executive branch that does not receive tax dollars for our operations presents unique requirements and restrictions, but also potentially mitigates some of the financial risk that would otherwise be associated with a cash shortfall. With annual total revenue in 2017 of approximately $70 billion, a financially-sound Postal Service continues to be vital to U.S. commerce.

The U.S. economy benefits greatly from us and the many businesses that provide the printing and mailing services that we support. Disruption of the mail would cause undue hardship to businesses and consumers as it would significantly inhibit the remittance of payments through the mail, and in the event of a cash shortfall, the U.S. government would likely prevent us from significantly curtailing or ceasing operations. We continue to inform the Administration, Congress, the PRC and other stakeholders of the immediate and long-term financial challenges we face and the legislative and regulatory changes that are required to restore our financial stability.

LEGISLATIVE, REGULATORY AND RELATED MATTERS

LEGISLATIVE UPDATE
As a self-funded independent establishment of the executive branch, our business model and operations are significantly influenced by congressional oversight and legislation. Additionally, Congress intended for us to be governed by an eleven-member Board of Governors ("Board") which generally consists of our Postmaster General, Deputy Postmaster General and nine independent governors ("Governors"). The Governors are appointed by the President with the advice and consent of the Senate. We have no presidentially appointed, Senate-confirmed Governors currently in office.

Appropriations
On June 13, 2018, the House Appropriations Committee approved the *Financial Services and General Government Act, 2019* (H.R. 6258), which includes $58,118,000 in funding for free mail for the blind and overseas voting. Representative David Joyce (R-OH) introduced an amendment to restore our 2012 service standards for *First-Class Mail* and *Periodicals*, which was passed by a voice vote and included in the bill. The bill also requires continuation of six-day delivery and prohibits any of the appropriated funds from being used to consolidate or close small rural or other small Post Offices. On July 19, 2018, the House passed the appropriations bill, which had been combined with the *Department of the Interior, Environment, and Related Agencies Appropriations Act, 2019* (H.R.6147).

On June 21, 2018, the Senate Appropriations Committee approved the *Financial Services and General Government Appropriations Act, 2019* (S. 3107), which includes $55,235,000 in funding for free mail for the blind and overseas voting. The six-day delivery frequency provision remains in the bill. No amendments regarding a service standard rollbacks for *First-Class Mail* and *Periodicals* were offered. On August 1, 2018, the Senate passed the four-bill spending package (H.R. 6147) that included the Financial Services bill.

Postal Service Reform

As previously reported, on March 16, 2017, the House Oversight and Government Reform Committee passed the *Postal Service Reform Act of 2017* (H.R. 756 - 115th Congress) with a single dissenting vote. The core provisions of the bipartisan measure would institute separate, Postal Service-only plans within FEHB that are fully integrated with Medicare, require Postal Service-specific demographic and economic assumptions in calculating pension liabilities, reinstate half of the exigent surcharge and authorize the provision of non-postal services to state, local and tribal governments. The measure would also reduce the number of Governors from nine to five, clarify their duties and allow them to set their own quorum requirements.

On June 12, 2018, the Postal Service reform bill was reintroduced as the *Postal Reform Act of 2018* (H.R. 6076), with Subcommittee on Government Operations Chairman Mark Meadows (R-NC) as the lead sponsor. The reintroduced bill is identical to the previous bill and was referred to the House Oversight and Government Reform, Energy and Commerce, and Ways and Means Committees.

On March 22, 2018, Senator Thomas Carper (D-Del) introduced the *Postal Service Reform Act of 2018* (S. 2629 - 115th Congress). The bipartisan measure would institute separate, Postal Service-only plans within FEHB that are integrated with Medicare. It would also establish a lump-sum payment from the PSRHBF to Medicare funds, in an amount equal to the ten-year increase in Medicare expenditures due to the bill's Medicare integration provisions. The lump-sum requirement would begin the first fiscal year beginning with 2021 in which the PSRHBF has assets above the 80% funding level provided for by the bill. Additionally, the measure would reinstate half of the temporary exigent rate increase, establish a moratorium of at least two years on service standard changes, and modify or defer rate-regulation reforms concerning products that do not fully cover costs like *Periodicals* and *Marketing Mail Flats*. The bill includes governance reforms that would reduce the number of Governors from nine to five, clarify their duties, and allow them to set their own quorum requirements. The measure would also authorize us to ship beer, wine, and distilled spirits and to partner with state and local governments in offering government services. S. 2629 has been placed on the Senate Legislative Calendar and awaits Senate floor action.

Board of Governors Nominations

On April 18, 2018, the Senate Homeland Security and Governmental Affairs Committee ("Committee") held a hearing to consider the nominations of the following individuals to serve on our Board:

- Calvin R. Tucker for the remainder of a term expiring December 8, 2023.
- Robert M. Duncan for the remainder of a seven-year term expiring December 8, 2018, and an additional term expiring December 8, 2025.
- David Williams for the remainder of a seven-year term expiring December 8, 2019.

On May 7, 2018, the Committee voted favorably to advance the nominations of Messrs. Duncan and Williams for consideration by the full Senate. Mr. Tucker's nomination is pending further Committee action.

TASK FORCE ON THE UNITED STATES POSTAL SERVICE

On April 12, 2018, the President issued Executive Order 13829 to establish a *Task Force on the United States Postal Service* ("Task Force"), to be chaired by the Secretary of the Treasury, as Secretary and as Chairman of the FFB, or his designee, to evaluate the operations and finances of the Postal Service. In addition to the Task Force Chair, the Task Force is composed of the Director of the Office of Management and Budget and the Director of OPM, or their designees. The Task Force shall conduct a thorough evaluation of the operations and finances of the Postal Service, including:

- The expansion and pricing of the package delivery market and the Postal Service's role in competitive markets;
- The decline in mail volume and its implications for Postal Service self-financing and the Postal Service monopoly over letter delivery and mailboxes;
- The definition of the "universal service obligation" in light of changes in technology, e-commerce, marketing practices, and customer needs;
- The Postal Service's role in the U.S. economy and in rural areas, communities, and small towns; and

- The state of the Postal Service business model, workforce, operations, costs, and pricing.

The Task Force, acting through the Chair and the Director of the Office of Management and Budget, shall submit a report to the President, in coordination with the Directors of the Domestic Policy and National Economic Councils, not later than 120 days after the date of the order (i.e., August 10, 2018).

FAIR VALUE MEASUREMENTS

As required by authoritative accounting literature, certain fair value disclosures for the periods ended June 30, 2018, and September 30, 2017, are contained in *Item 1. Financial Statements*, *Notes to Unaudited Financial Statements*. We did not recognize gains as a result of valuation measurements during the three and nine months ended June 30, 2018. All recognized losses have been incorporated into our financial statements as of June 30, 2018. See *Item 1. Financial Statements*, *Notes to Unaudited Financial Statements*, *Note 10 - Fair Value Measurement.*

RELATED PARTY TRANSACTIONS

As disclosed throughout this quarterly report, we have significant transactions with other U.S. government entities, which are considered related parties for reporting purposes. For a more detailed description, see *Item 1. Financial Statements*, *Notes to Unaudited Financial Statements*, *Note 3 - Related Parties*.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The preparation of financial statements in accordance with GAAP requires management to make significant judgments and estimates to develop certain amounts reflected and disclosed in the financial statements. In many cases, alternative policies or estimation techniques may be used.

We maintain a thorough process to review the application of accounting policies and to evaluate the appropriateness of the many estimates that are required to prepare the financial statements of a large organization. However, even under optimal circumstances, estimates routinely require adjustment based on changing circumstances and new or better information.

The accounting policies deemed either the most judgmental or which involve the selection or application of alternative accounting policies, and are material to the interim financial statements, are described in *Critical Accounting Estimates* contained in *Management's Discussion and Analysis of Financial Condition and Results of Operations* of the Annual Report. Management normally discusses the development and selection of accounting policies and estimates with the Audit and Finance Committee of the Board (the "Audit Committee"). Given that we currently have no Governors, the Audit Committee is not currently functioning as designed, and the Temporary Emergency Committee of the Board is responsible for making decisions with respect to audit and finance matters that are within its authority.

RECENT ACCOUNTING STANDARDS

See *Item 1. Financial Statements*, *Notes to Unaudited Financial Statements*, *Note 1 - Basis of Presentation*, *Recent Accounting Standards* for a description of recently announced accounting standards.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

In the normal course of business we are exposed to market risks from changes in commodity prices, certain foreign currency exchange rates and interest rates. Our commodity price risk consists primarily of exposure to changes in prices for diesel fuel, unleaded gasoline and aircraft fuel for transportation of the mail, and fuel for heating facilities. We have foreign currency risk related to the settlement of terminal dues and transit fees with foreign postal administrations for international mail.

We have not used derivative commodity or financial instruments to manage market risk related to commodities, foreign currency exchange or interest rate fluctuations for debt instruments. Additionally, we do not purchase or hold derivative financial instruments for speculative purposes.

We also have provisions in our debt agreements that allow us to prepay our $15.0 billion debt at any time at a price determined by the Secretary of the Treasury, based on prevailing interest rates in the U.S. Treasury market at the time of repayment.

See *Item 7A. Quantitative and Qualitative Disclosures about Market Risk* in the Annual Report for additional information.

ITEM 4. CONTROLS AND PROCEDURES

Management is responsible for the preparation, integrity and fair presentation of our financial statements.

DISCLOSURE CONTROLS

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in quarterly and annual reports is recorded, processed, summarized, and reported within the time frames specified by PAEA, and that this information is accumulated and communicated to our management, including the Postmaster General and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

We carried out an evaluation under the supervision and with the participation of management, including the Postmaster General and the Chief Financial Officer, of the effectiveness of the design and operation of disclosure controls and procedures as of June 30, 2018. Based upon and as of the date of the evaluation, the Postmaster General and the Chief Financial Officer concluded that our disclosure controls and procedures were effective.

INTERNAL CONTROLS

We have made no changes in our internal control over financial reporting during the three months ended June 30, 2018, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

For a discussion of legal proceedings affecting us, please refer to *Item 1. Financial Statements*, *Notes to Unaudited Financial Statements* and *Note 6 - Commitments and Contingencies*, as well as our Annual Report.

ITEM 1A. RISK FACTORS

No material changes have transpired in our risk factors from those disclosed in *Item 1A. Risk Factors* of our Annual Report.

ITEM 5. OTHER INFORMATION

On August 3, 2018, our Vice President, Controller and Chief Accounting Officer, Maura McDevitt, announced that she has accepted a position with another organization and will be resigning from the Postal Service effective August 24, 2018. As of the date of this filing, her replacement has yet to be named.

ITEM 6. EXHIBITS

Exhibit Number	Description
31.1	Certification of Principal Executive Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the *Securities and Exchange Act of 1934*, as Adopted Pursuant to Section 302 of the *Sarbanes-Oxley Act of 2002*.
31.2	Certification of Principal Financial Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the *Securities and Exchange Act of 1934*, as Adopted Pursuant to Section 302 of the *Sarbanes-Oxley Act of 2002*.
32.1	Certification of Principal Executive Officer Pursuant to *18 U.S.C. Section 1350*, as Adopted Pursuant to Section 906 of the *Sarbanes-Oxley Act of 2002*.
32.2	Certification of Principal Financial Officer Pursuant to *18 U.S.C. Section 1350*, as Adopted Pursuant to Section 906 of the *Sarbanes-Oxley Act of 2002*.

Signatures

Pursuant to the requirements of the *Postal Accountability and Enhancement Act of 2006*, the United States Postal Service has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

United States Postal Service

/s/Megan J. Brennan
Megan J. Brennan
Postmaster General and Chief Executive Officer

Date: August 8, 2018

/s/Joseph Corbett
Joseph Corbett
Chief Financial Officer and Executive Vice President

Date: August 8, 2018

Exhibit 31.1

CERTIFICATION PURSUANT TO
RULES 13a-14(a) AND 15d-14(a) UNDER THE SECURITIES AND EXCHANGE ACT OF 1934,
AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002.

I, Megan J. Brennan, certify that:

1. I have reviewed this quarterly report on Form 10-Q of the United States Postal Service ("Postal Service");

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the Postal Service as of, and for, the periods presented in this report;

4. The Postal Service's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the Postal Service and have:

    a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Postal Service, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

    b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

    c. Evaluated the effectiveness of the Postal Service's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

    d. Disclosed in this report any change in the Postal Service's internal control over financial reporting that occurred during the Postal Service's most recent fiscal quarter (the Postal Service's fourth fiscal quarter in the case of an Annual Report) that has materially affected, or is reasonably likely to materially affect, the Postal Service's internal control over financial reporting; and

5. The Postal Service's other certifying officer and I have disclosed based on our most recent evaluation of internal control over financial reporting, to the Postal Service's independent registered accounting firm and the Audit and Finance Committee of the Postal Service's Board of Governors (or persons performing the equivalent functions):

    a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Postal Service's ability to record, process, summarize and report financial information; and

    b. Any fraud, whether or not material, that involves management or other employees who have significant role in the Postal Service's internal control over financial reporting.

Date: August 8, 2018

/s/Megan J. Brennan

Megan J. Brennan

Postmaster General and Chief Executive Officer

Exhibit 31.2

CERTIFICATION PURSUANT TO
RULES 13a-14(a) AND 15d-14(a) UNDER THE SECURITIES AND EXCHANGE ACT OF 1934,
AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002.

I, Joseph Corbett, certify that:

1. I have reviewed this quarterly report on Form 10-Q of the United States Postal Service ("Postal Service");
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the Postal Service as of, and for, the periods presented in this report;
4. The Postal Service's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the Postal Service and have:
    a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Postal Service, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
    b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
    c. Evaluated the effectiveness of the Postal Service's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
    d. Disclosed in this report any change in the Postal Service's internal control over financial reporting that occurred during the Postal Service's most recent fiscal quarter (the Postal Service's fourth fiscal quarter in the case of an Annual Report) that has materially affected, or is reasonably likely to materially affect, the Postal Service's internal control over financial reporting; and
5. The Postal Service's other certifying officer and I have disclosed based on our most recent evaluation of internal control over financial reporting, to the Postal Service's independent registered accounting firm and the Audit and Finance Committee of the Postal Service's Board of Governors (or persons performing the equivalent functions):
    a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Postal Service's ability to record, process, summarize and report financial information; and
    b. Any fraud, whether or not material, that involves management or other employees who have significant role in the Postal Service's internal control over financial reporting.

Date: August 8, 2018

/s/Joseph Corbett

Joseph Corbett

Chief Financial Officer and Executive Vice President

Exhibit 32.1

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002.

In connection with the Quarterly Report of the United States Postal Service (“Postal Service”) on Form 10-Q for the period ended June 30, 2018, (the “Report”), I, Megan J. Brennan, certify, pursuant to *18 U.S.C. Section 1350*, as adopted pursuant to Section 906 of the *Sarbanes-Oxley Act of 2002* that:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the *Securities Exchange Act of 1934*; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Postal Service.

Dated: August 8, 2018

/s/Megan J. Brennan

Megan J. Brennan

Postmaster General and Chief Executive Officer

Exhibit 32.2

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002.

In connection with the Quarterly Report of the United States Postal Service ("Postal Service") on Form 10-Q for the period ended June 30, 2018, (the "Report"), I, Joseph Corbett, certify, pursuant to *18 U.S.C. Section 1350*, as adopted pursuant to Section 906 of the *Sarbanes-Oxley Act of 2002* that:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the *Securities Exchange Act of 1934*; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Postal Service.

Dated: August 8, 2018

/s/Joseph Corbett
Joseph Corbett
Chief Financial Officer and Executive Vice President